Palestine Investment Fund
Annual Report 2003

C O N T E N T S




Dedication to President Yasser Arafat

The 2003 Annual Report of the Palestine Investment Fund is dedicated with pride to His Excellency Yasser Arafat, Chairman of the Palestinian National Authority and the leader of the Palestinian people. This report was made possible by his clear vision for the PIF, his determination to serve his people, and his perseverance in the face of many obstacles. We are deeply indebted to him for his support of the PIF's work.

PALESTINE LIBERATION ORGANIZATION
Palestine National Authority
Office of the President

منظمة التحرير الفلسطينية
السلطة الوطنية الفلسطينية
مكتب الرئيس

قرار رقم (   ) لسنة 2002

إن رئيس دولة فلسطين
رئيس اللجنة التنفيذية لمنظمة التحرير الفلسطينية
رئيس السلطة الوطنية الفلسطينية

وبناءً على الصلاحيات المخولة له
وتحقيقاً لمقتضيات المصلحة العامة
يقرر مايلي:-

مادة(1): يشكل مجلس إدارة صندوق الاستثمار الفلسطيني على النحو التالي:-

1- السيد د. سلام فياض	رئيساً لمجلس الإدارة	- وزير المالية.
2- السيد صبيح المصري	نائباً للرئيس	- ممثلاً للقطاع الخاص.
3- السيد ماهر المصري	عضواً	- وزير الاقتصاد والتجارة والصناعة.
4- السيد محمد رشيد	عضواً	- مديراً عاماً للصندوق.
5- السيد سامر خوري	عضواً	- ممثلاً للقطاع الخاص.
6- السيد طلال ناصرالدين	عضواً	- ممثلاً للقطاع الخاص.
7- السيد عزام الشوا	عضواً	- ممثلاً للقطاع الخاص.

مادة (2): على جميع الجهات المختصة، كل فيما يخصه، تنفيذ هذا القرار ويعمل به من تاريخ صدوره، وينشر في الجريدة الرسمية.

صدر في مدينة رام الله بتاريخ: 2002/8/14م.

ياسر عرفات
رئيس دولة فلسطين
رئيس اللجنة التنفيذية لمنظمة التحرير الفلسطينية
رئيس السلطة الوطنية الفلسطينية

CHAIRMAN'S STATEMENT

"The establishment of the Palestinian Investment Fund in 2000 stands as a benchmark event in the process of regaining the trust of the Palestinian people."

The early years of the Palestinian National Authority's governance of the West Bank and Gaza Strip have not been easy ones. From the outset, the PNA has been engaged in a daily struggle to cope with the ongoing Israeli occupation, the all-absorbing demands of political negotiations, a paralyzed economy, and the frustrations of thwarted initiatives and dashed hopes.

The brunt of this struggle has been borne first and foremost by the Palestinian people, who have endured the unendurable for years on end... restrictions on movement, acute physical and emotional distress, mounting financial losses. The unfortunate result has been a growing crisis of confidence and deterioration in the foundation of trust upon which all governments are built.

Creation of the PIF

While recognizing the critical importance of remaining engaged in the political arena, the Palestinian Authority began taking steps to reestablish and underscore its longstanding commitment to good governance, which was becoming obscured in the haze of the ongoing struggle for national self-determination. The establishment of the Palestinian Investment Fund in 2000 stands as a benchmark event in the process of regaining the trust of the Palestinian people.

This first Annual Report of the Palestinian Investment Fund for fiscal year 2003 presents a full accounting and valuation of the assets of the Palestinian Authority. The PIF portfolio was created by transferring and consolidating all commercial assets and investment holdings previously managed by the Palestinian Authority, as required by and in full compliance with the directive issued by the Palestinian Ministry of Finance.

Regain Trust, Restore Hope

As Chairman of the Board, it is my responsibility, together with my Board colleagues, to ensure that the information contained in these pages is both comprehensive and accurate. The publication of these financial reports, and the certifications contained in the accompanying statements by Standard & Poor's, The Democracy Council and Ernst & Young, is an accomplishment the entire Board looks to with great pride.

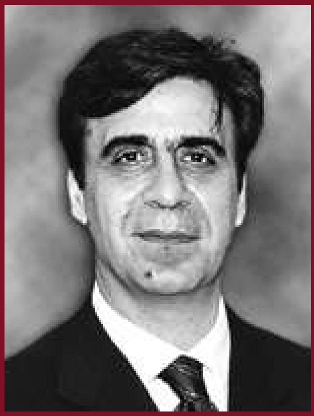
In today's troubled times, it may be difficult to find signs of hope, but they are there. The 2003 PIF Annual Report is only one in a series of significant advances on the road to full restoration of confidence and trust in Palestinian governance. Restructuring efforts are underway in virtually all Palestinian ministries, and a constructive public/private sector dialogue is gaining momentum in every sector of the Palestinian economy.

On behalf of the PIF Board of Directors, I extend my sincere thanks to President Yasser Arafat and my colleagues in the Palestinian Authority for their continuing support of our work. I also thank my fellow PIF Board members for their dedicated service to the Palestinian people. We will continue to face the challenges that confront us with resolve and determination. We will not rest until we have succeeded in our efforts to regain the people's trust, to improve confidence in the prospects of the Palestinian Economy, and renew hope in the possibilities of a better future.

Dr. Salam Fayyad
Minister of Finance and PIF Chairman
01 May 2004

REPORT FROM THE CHIEF EXECUTIVE OFFICER

"The PIF's studied approach has produced a ratio of gain to loss praised by our external oversight entities"



Maintaining a profitable investment portfolio is a challenging task in the best of economic times. The atmosphere of volatility plaguing the world's financial markets began in 2001, and persists until today. Investors large and small struggle to cope with the market repercussions of corporate upheavals in the United States, the war in Iraq and the consuming international debate over the Palestinian struggle.

PIF Goals

The Palestinian Investment Fund portfolio represents the assets held in trust by the Palestinian National Authority for the benefit of the Palestinian people. The PIF's Board of Directors is vested with the authority, and the solemn responsibility, to manage these assets wisely. Our objective is to generate socio-economic development in Palestine and to raise the standard of living for the average Palestinian through a strategy of proactive investment in viable opportunities across all economic sectors and in infrastructure improvement projects.

Risk Management

Risk is inherent in the investment process. Money managers engage in a daily process of monitoring the level of risk present in their portfolios, which rises and falls in concert with a wide-ranging scope of political, economic and social events throughout the world. Short-term losses are measured against potential long-term gains, and decisions must be made using the best financial information at hand whether to stay the course, change strategy or dispose of non-performing assets.

The generally positive economic conditions that prevailed at the time the PIF was established in 2002 are dramatically different from those we face today. It is under conditions such as these, however, that the value and impact of the PIF's clearly defined mission, its prudent, systematic investment strategy and the collective expertise of its board members are most clearly seen. Our management team applies very strict adherence to our established policies and procedures resulted in a strong overall performance record for the PIF portfolio. The opportunity remains for under-performing assets to rebound in time.

Board Qualifications

The PIF Board of Directors distinguished group of individuals whose cumulative wealth of experience is seconded only by its commitment to the economic advancement of the Palestinian people. Every member of the Board of Directors brings a unique set of skills and qualifications to the task of creating PIF investment strategy, including large scale corporate management, commercial banking, institutional investing and cabinet-level government experience, as is evidenced by the biographies included later in these pages. Each one is highly knowledgeable of the intricate political, legal and economic considerations that are the realities of Palestinian life.

2003 Annual Report

The 2003 PIF Annual Report is the first public report on the achievements of the Board's investment strategy. It also represents one of the first reports of its kind to be published by a developing nation - a completely voluntary, comprehensive, accurate disclosure of its financial assets. The PIF's studied approach has produced a ratio of gain to loss praised by our external oversight entities: Standard & Poors, the Democracy Council and the international accounting and auditing firm Ernst & Young.

As Chief Executive Officer and Managing Director of PIF, it gives me great pride to submit this record of performance and achievement to the Palestinian people. Assuring you of our commitment to execute our responsibilities, collectively and individually, to the utmost of our ability.

Mohamed Rachid
Chief Executive Officer and Managing Director
01 May 2004

BOARD OF DIRECTORS

Dr. Salam Fayyad

Palestinian Minister of Finance
Chairman of the Board

Sabih Masri

Vice Chairman of the Board

Maher Masri

Palestinian Minister of National Economy, PIF Board Member

Dr. Salam Fayyad

Dr. Fayyad was appointed Chairman of the Palestine Investment Fund in 2002. He heads the PIF's Audit Committee and currently serves as the Minister of Finance of the Palestinian National Authority.

Previously Dr. Fayyad held the post of Resident Representative of the International Monetary Fund (IMF) in the West Bank and Gaza Strip. He also served as Regional Manager for the Arab Bank PLC in Palestine for a brief period in 2002, preceding his appointment as PNA Minister of Finance. At prior points in his career, Dr. Fayyad held teachings and research assignments at the University of Texas at Austin and Yarmuk University in Jordan. He also served as a visiting scholar at the Federal Reserve Bank of St. Louis.

Dr. Fayyad received a Bachelor degree in Science from the American University of Beirut in 1975, an MBA from St. Edward's University in 1980 and a Ph.D. in Economics from the University of Texas at Austin in 1986

Sabih Masri

Sabih Masri was appointed Vice Chairman of the Palestine Investment Fund's Board of Directors in 2002. He chairs the Nominations Committee and also serves on the fund's Investment Committee.

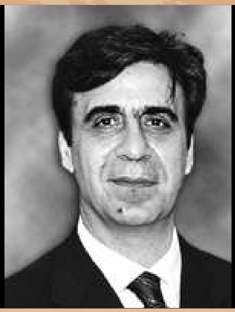
Vice Chairman Masri, an internationally respected business executive, founded and presently manages investment companies and financial economic institutions active in Palestine and throughout the region. His private sector affiliations in Palestine and abroad include the Arab Supply and Trading Corporation (ASTRA), Zara Investment, Cairo Amman Bank and the Rum Agricultural Company.
Mr. Masri played an active role in the establishment of PADICO, the Palestine Investment and Development Company, and currently serves on its Board of Directors. He is Chairman of the Board of the Palestinian Telecommunications Company (PALTEL), and a founder and Chairman of the Board of Directors of the Palestine Securities Exchange (PSE) in Nablus. He is also a member of the Board of Directors of the Arab Bank PLC. Mr. Masri's diverse business interests span a variety of economic sectors, including agriculture, hospitality and tourism, trade, manufacturing, general contracting and construction.

Maher Masri

Minister Maher Masri was appointed to the Board of the Palestine Investment Fund in 2002 and currently chairs the PIF's Investment Committee. He presently serves as Minister of National Economy for the Palestinian National Authority.

Minister Masri is a dedicated proponent of the promotion of a constructive public-private sector dialogue in Palestine, and in that capacity has spearheaded the creation of a number of influential Palestinian trade associations and industry forums such as the Palestinian Trade Center (PALTRADE), the Palestinian IT Association (PITA), and the Private Sector Coordinating Council. Minister Masri also serves as Chairman of the Board of the Palestinian Investment Promotion Agency (PIPA), the Palestinian Industrial Estates and Free Zones Area (PIEFZA), and the Palestinian Banking Corporation (PBC), a development bank created to stimulate economic growth in Palestine.

Minister Masri holds his Bachelor and Master of Arts degrees in Economics from the American University in Beirut, Lebanon.



Mohamed Rachid

Chief Executive Officer and Managing Director

Samer Khoury

PIF Board Member

Talal Nasiruddin

PIF Board Member

Jawdat Khoudary

PIF Board Member

Mohamed Rachid

Mohamed Rachid was appointed to the post of Chief Executive Officer and Managing Director for the Palestine Investment Fund in 2002. He serves as a member of the Audit Committee, the Investment Committee, the Conflicts Committee and the Nominations Committee.

Mr. Rachid serves as Board Liaison between the PIF management team and the Board of Directors. His diverse responsibilities include oversight of PIF project management operations in all of the fund's investment areas.

Previously, Mr. Rachid held the post of Managing Director and Chairman of the Board of Directors for the Palestine Commercial Services Company (PCSC), the organizational predecessor of the Palestine Investment Fund. PCSC's investment portfolio includes interests in a wide range of economic sectors, including hospitality/tourism, insurance, construction, real estate, power utilities, telecommunications, consumer products, aviation and aviation facilities management. The PCSC's holdings and investment management activities laid the groundwork for the creation of profitable economic partnerships between the Palestinian public and private sectors and the international investment community.

Samer Khoury

Samer Khoury was appointed to the Board of Directors of the Palestine Investment Fund in 2002. He serves on its Audit and the Nominations Committees.

Mr. Khoury is the Executive Vice President of Operations of the CCC Group. His responsibilities include oversight of the marketing and management operations of the CCC Group's worldwide business interests. Consolidated Contractors Company (CCC) is one of the region's largest international construction companies, operating throughout the Middle East, Africa, Europe and the United States.

From 1987 through 1990, Mr. Khoury managed CCC's Kuwaiti operations, which generated over $50 million in revenues annually and employed more than 1,000 permanent staff. CCC has played an important role in Palestinian infrastructure development. Its key areas of investment include the construction of the Gaza power plant, exploration for offshore natural gas reserves in Gaza (a joint venture with multinational British Gas), various housing development initiatives in Gaza, and hospitality and tourism sector investments in Bethlehem.

Talal Nasiruddin

Talal Nasiruddin was appointed as a Member of the Board of the Palestine Investment Fund in 2002. He currently serves as Chairman of the Conflicts Committee and as a member of the Investment and Nominations Committees.

Mr. Nasiruddin is currently the Chairman of the Board and Chief Executive Officer of the Birzeit Pharmaceutical Group, the largest pharmaceutical manufacturing entity in Palestine. He is a member of the Palestinian Federation of Industries, a national trade association of Palestinian industrial and manufacturing enterprises.

Mr. Nasiruddin also belongs to the Palestinian Businessmen's Association and is an active member of the Palestinian Private Sector Coordinating Council promoting constructive economic dialogue between the public and private sectors.

Jawdat Khoudary

Mr. Jawdat Khoudary was appointed to the Board of Directors of the Palestine Investment Fund in 2003*. He is a member of the Audit, Investment, Conflicts and Nominations Committees.

Since 1987, Mr. Khoudary has served as Chairman of the Board for the Saqa and Khoudary Contracting Company, one of the largest contracting firms operating in the West Bank and Gaza Strip. His contracting group made significant contributions to landmark infrastructure development projects in Palestine, including construction of a power station in Gaza, the Bethlehem 2000 tourism sector projects funded by the United States Agency for International Development (USAID), and the Salah Al-Deen Street development initiative in Gaza.

Mr. Khoudary also chairs the Board of Directors of Al-Nasr Industries for the Manufacturing of Construction Steel, an ISO 9002 Company.

**Mr. Khoudary replaced former PIF Board Member Azzam Shawwa, who resigned his position on the Board to assume a cabinet level appointment in the Palestinian National Authority.*

The Palestine Investment Fund (PIF) promotes the stable growth of the Palestinian economy by stimulating Palestinian private sector investment, both domestic and foreign, and by encouraging the development of the national infrastructure needed for sustainable economic prosperity. The PIF also provides responsible stewardship of the assets and holdings of the Palestinian National Authority.

MISSION STATEMENT

The PIF's mission is to serve as a catalyst for socio-economic development in Palestine, and to raise the standard of living for the average Palestinian by placing capital and expertise in strategically important and under serviced sectors.

BACKGROUND

The PIF was created on October 14, 2000 by decree of His Excellency Yasser Arafat, President of the Palestinian National Authority. It is comprised of a 7-member Board of Directors headed by Chairman Salam Fayyad, Palestinian Minister of Finance.

As one of its first tasks, the PIF took on the responsibility of valuing and publishing a comprehensive public record of the assets and investments held by the Palestinian National Authority, assisted by the international agencies of Standard & Poors, the Democracy Council and the international accounting firm of Ernst & Young. All investment assets and commercial holdings of the PNA were transferred to and consolidated under the management of the PIF. As the valuation process advanced, the PIF created a web site (www.palestineinvestmentfund.com) in order to make available to the general public each valuation report as it was completed.

The web site also provides detailed information regarding the fund's structure and management practices, including its Articles of Incorporation, Policies and Procedures, and Transparency Diagnostic Methodology. Biographies of each of the 7 Board members are also available online, as well as an archive of the organization's press releases and media coverage.

Jacir Palace Hotel - Bethlehem

Plaza Mall - Albireh

Intercontinental Jericho

Grand Park Hotel - Ramallah

Natural Gas - Gaza

Paltel Building - Nablus

American School - Gaza

Orascom Telecom

Gaza Power Plant

MOVING FORWARD

"The PIF's goals are far-reaching, but achievable"

Statement of PIF Investment Committee Chairman
Minister of National Economy
Maher Masri

In spite of the short-term setbacks imposed by recent global and local economic slowdowns and the scarcity of prime investment opportunities, the PIF has an established long-term commitment to socio-economic development and to the betterment of living standards for Palestinian citizens. Our goals are far-reaching, but achievable.

The PIF Board has taken up a challenge. We intend to fulfill our mandate to improve the economic standing of a country suffering from prolonged paralysis imposed by Israeli occupation.

The PIFís guiding principles are specific with regard to the composition of its portfolio, management structure, conflict of interest policy, and evaluation methodology for asset performance. They conform to internationally-accepted best practices and serve as the foundation upon which the PIF will act to realize its vision of facilitating economic expansion and improving the quality of life for our people.

As we seek promising investment opportunities to help us reach our goals, the PIF maintains rigorous standards for its existing projects, all of which must demonstrate profitability and sustainability in a highly adverse economic climate. Our diversified local, regional and international portfolio protects us from prolonged downturns in any one economic sector or geographic area of the world. We strive to maintain a consistently profitable balance between manageable risk and reasonable rate of return on every investment. As the portfolio grows, we identify new investment opportunities that will contribute to the stable growth of our economy.

PIF investment strategy targets projects in the areas of education, health, technical and scientific research and infrastructure development, after performing proper due diligence to encourage private sector participation. The PIF does not invest in any small or microenterprise projects. We do not compete with the private sector in Palestine in any economic sector where the private sector has traditionally taken an active participating role. The PIF actively promotes a constructive economic dialogue between the Palestinian public and private sectors, and strives to eliminate areas of functional overlap or non-productive competition.

The private sector is doing its part as well, working to improve both the quantity and quality of its services and products. The PIF aims to work in partnership with the private sector, actively promoting joint participation in mid to large-size economic development projects which would otherwise be beyond the scope of the private sector, mainly due to significant initial capital outlay requirements and high risk factors. In this way, we will help the private sector to minimize investment risk, boost overall economic development and encourage foreign and domestic investment in Palestine.

The PIF, through its investment policy, seeks to build economic self-reliance by bolstering trade activity, stimulating the labor market and raising sector productivity. This strategy should help strengthen the private sectorís confidence in the future of the Palestinian economy and increase investment.

On behalf of the PIF Board of Directors and as Chairman of the Investments Committee, I reiterate our commitment to the growth of the Palestinian private sector. Their trust and support has been instrumental in helping us develop long-term growth strategies for the economy as a whole. We look forward to a successful and productive partnership for many years to come.

Maher Masri
Minister of National Economy
Chairman, PIF Investment Committee
01 May 2004

INVESTMENT STRATEGY
As of January 2004

Introduction & *Investment Principles*

The PIF investment strategy was prepared through the joint efforts of the Fund management and the Board of Directors Investment Committee. It is the investment plan to be formulated and agreed upon by the Board of Directors and implemented by the management based on the required governance and in particular the approval of the Investment Committee.

The investment strategy is based upon:

1. Investment principles set by the Investment Committee & the Fund management.
2. Adherence to the Policies and Procedures of the PIF.
3. Asset allocation tables which will become future comparison reference as the investment strategy is periodically updated.
4. Current and future investment activities generated and being executed by the management in order to achieve implementation of the investment plan.

The Investment Committee meeting of the Board of Directors held in Cairo on September 24, 2003 set the principles and guidelines for the near future investment strategy based on the articles, policies and procedures of the PIF.

Perception & Outlook:

The investment strategy is primarily dependant upon forming a clear investment perspective for the Fund to act as its logical founding backbone and to be adhered to by all its employees. The general aim of the fund is to participate in the socio-economic development of Palestine and to raise the standard of living of the average Palestinian through the fund's involvement in various economic development sectors as well as infrastructure based projects, based on the following:

1. The fund shall not compete with the private sector in Palestine in any and all economic investment sectors where the private sector has traditionally taken an active participating role and within its financial capabilities.
2. Gradual withdrawal from existing projects relevant to paragraph one above within the concept of privatization and according to a timely business plan.
3. The fund shall not invest in small or microeconomic projects.

INVESTMENT STRATEGY

As of January 2004

4. Fund investments shall be made following proper due diligence procedures in mid to large size economic development projects which are beyond the scope of the private sector mainly due to its significant initial capital outlay and high risk factor to encourage the private sector's participation in this endeavor.

5. Invest in projects that principally aim to improve the social, economic and educational standard in Palestine as is the case with medical and educational facilities.

6. The fund shall play a leading role in investing in Palestinian infrastructure projects after performing proper due diligence in order to encourage private sector participation.

7. The Fund shall refrain from complete ownership of any given investment.

8. The Fund shall invest in foreign markets and in growth oriented industries to increase the Fund's financial resources whereby a current 50-50 mix between investments inside and out of Palestine.

9. Continuously monitor industries with high growth potential in emerging markets so as to determine optimum entry and exit strategies and to capitalize on such opportunities.

10. Perform in-depth fundamental and technical analysis and apply relevant risk management tools to reduce overall investment risk including but not limited to financial/industry/business/interest rate/exchange rate/inflation risk etc.

11. The Fund shall allocate a budget to assist the technical as well as scientific research establishments in Palestine to promote domestic economic development.

12. Adhere to stated asset allocation percentages as per the Fund's Policies and Procedures.

13. Periodic monitoring and re-evaluation of the Fund's investment strategy between the Investment Committee, Board of Directors and the Fund's Management.

14. Not to participate in the executive management of any Investment Project.

15. Support non Performing Distressed Companies.

16. To participate in supporting the development of the Housing Sector.

PRIVATE SECTOR PERSPECTIVE

"PIF's role in the expansion of the Palestinian economy will grow in the coming years as it takes on more far-reaching goals vis-à-vis the Palestinian economy, private sector and the community at large."

2003 was not a year of progress and economic success in general; thankfully, however, it was not worse than previous years. In spite of losses that struck most economic sectors hard, the Palestinian private sector has recorded a number of successes in different areas.

Under a truly adverse set of conditions, the Palestine Investment Fund (PIF) diligently pursued its investment goals based on conservative, precise strategies designed to minimize risk and maximize return on investment. We redirect returns from profitable assets to underserved sectors, working to improve Palestinian economic performance by helping capital investors and private sector concerns bear investment risk under the most volatile conditions. The PIF identifies vital projects in need of public sector assistance, providing support until they mature and are able to pursue success on their own.

The PIF is committed to the economic growth of Palestine. We hope to serve as the developmental and economic catalyst whose joint public/private sector activities will establish a solid investment base in the Palestinian market. PIF also aims to actively counter the negative repercussions of the current political situation by adopting policies that expand investment, encourage privatization and reinforce the vision of shared public/private sector leadership in the strengthening of our market economy. Palestine's private sector institutions have proven themselves most capable of shouldering this significant national economic responsibility.
PIF's role in the expansion of the Palestinian economy will grow in the coming years as it takes on more far-reaching goals vis-à-vis the Palestinian economy, private sector and the community at large. Many of its planned projects are as yet unimplemented and require careful attention and support. Progress and growth in some sectors will depend on the transfer of skills and technological expertise, and continued efforts to expand managerial and operational capacity. Perhaps the most pressing issue is the need to create tens of thousands of employment opportunities to replace those lost by the Israeli closure of its borders to Palestinian labor.

The PIF will fulfill its obligations with the support of all stakeholders seeking to build a better future for the Palestinians. A solid partnership is being forged between the private and public sectors. The private sector is being asked to invest both capital and experience in Palestine; an endeavor that will require professionalism, persistence and courage.

On behalf of PIF, I would like to extend deep gratitude to our leader, His Excellency Yasser Arafat, and to all the members of the Palestinian National Authority. I recognize and commend the PIF Board of Directors for their personal sacrifices of time and effort, and extend my thanks to its management staff for their professionalism and dedication. We look forward to even greater achievements in the future.

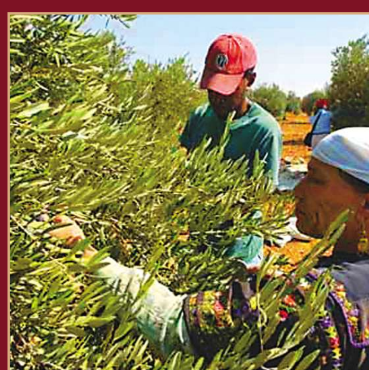
Samer Khoury
PIF Board Member
01 May 2004

OVERVIEW OF THE PALESTINIAN ECONOMY

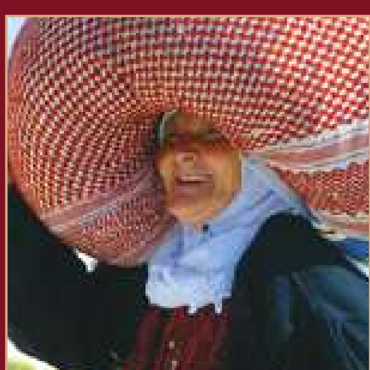
Education

Manufacturing

Labor Force



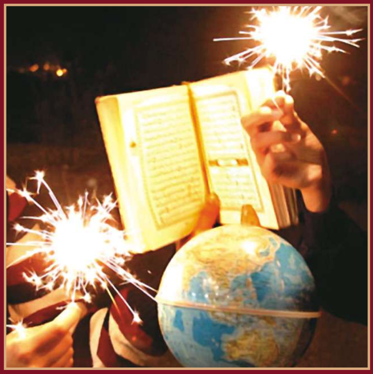
Agriculture



Population

Skilled Trades

Infrastructure



Tourism

OVERVIEW OF THE PALESTINIAN ECONOMY

After three years of entirely negative economic performance, the recent data on the Palestinian economy indicates a modest economic recovery. This conclusion was emphasized by the increase in the area of building starting in 2003[1] and the steady increase in new employment in both the West Bank and Gaza Strip during 2003[2]. On the other hand, recent data on foreign trade for the same period provides evidence of continued deterioration[3]. Likewise, the latest business confidence survey of April 2004[4] shows that the business community does not expect too much positive improvements in sales and investments. These contradicting signals of various indicators reflect the types of difficulties and obstacles which face the Palestinian economy. These are mainly man-made obstacles, with devastating impact on the economy from month to month, and are difficult to predict.

Population and Social Services Growth

Population Characteristics

The Palestinian population in the West Bank and Gaza Strip (WBGS), including East Jerusalem, reached 3.7 million by the end of 2003. Of the total, 2.356 million people are living in the West Bank and 1.365 million in the Gaza Strip. Palestine has a very high population growth rate, which rose to more than 4.5% during 1994 - 2003. As a result of this high growth, more than 50% of the population is under the age of 18, and the dependency rate is over six persons. These trends, while indicating a young and energetic society, can exert a negative impact on the quality of life for the whole population.

Latest poverty statistics[5] indicate improvements in the quality of life, and the ratio of those under poverty line in the Palestinian Territory decreased to 35.5% in December 2003. The rate of households who live under poverty line in Gaza is 44.7%, while the rate in the West Bank was 30.9% of all households.

Labor Force Characteristics

In the first quarter of 2004, there were 816,000 workers in the Palestinian labor force, compared to 735,000 in the 3rd quarter of 2003. The participating rate is equal to 40.1% of the total population aged 15 and above. The rate of participation in the labor force was lower than the pre-September 2000 level. As for the dependency ratio, the Labor Force Survey of January - March 2004 shows a remarkable increase from 4.8 in the 3rd quarter of 2000 to 6.3 in the 1st quarter of 2004.

Despite pressure on social and welfare services as a result of high population growth, Palestine continues to be characterized by its highly skilled labor force, clearly reflected in the level of schooling of Palestinian workers. The recent labor force survey showed that the percentage of workers who had completed 13 years or more of schooling has increased from 21.2% in 1998 to 31% in 2002, while the ratio of those who had not attended school decreased from 3.8% to 1.2% over the same period.

The structure of the Palestinian labor force according to type of occupation showed that 4.5% are legislators or senior officials and management, 23.7% are professionals, 18.7% work in services, retail and markets, 12.8% are skilled agricultural workers, 17.5 are craft and related trade workers, 8.6% are machine operators, and the ratio of those in elementary occupation is 14.2%.

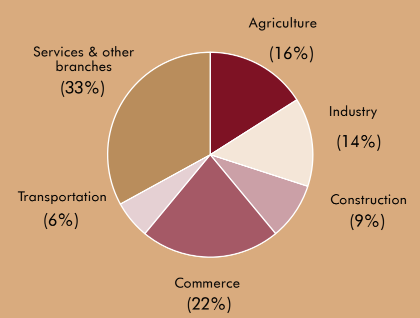
Recent employment data witnessed relatively steady growth in both the West Bank and Gaza Strip during 2003. The number of employed persons in the West Bank, which decreased from 352,000 in the third quarter of 2000of 2000 to 287,000 (lowest level) in the second quarter of 2002, increased to 387,000 in the fourth quarter of 2003.

Similarly, the number of employed persons in Gaza Strip decreased from 163,000 in the third quarter of 2000 to 111,000 (lowest level) in the third quarter of 2002, then increased to 180,000 in the third quarter of 2003 (the highest level) and slightly decreased to 173,000 as a result of increased political tension in the fourth quarter of 2003. A large number of the newly created jobs were in agriculture (24,000 in the West bank and 17,000 in Gaza), which might be affected by seasonal factors. The construction sector created 21,000 jobs in the West Bank and 11,000 jobs in Gaza, commerce created 17,000 jobs in the West Bank and 11,000 jobs in Gaza, services created 10,000 jobs in the West Bank and 14,000 jobs in Gaza, and the industrial sector created 9,000 jobs in the West Bank and 4,000 jobs in Gaza.

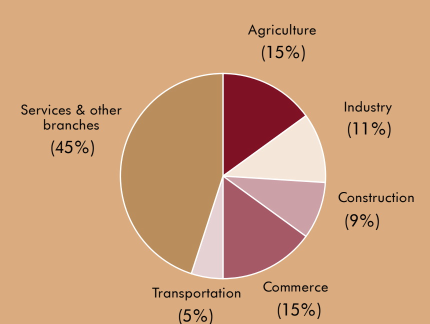
Employed persons aged 15 years and over by economic activity & place of work in first quarter 2004[6] (in thousands)

Economic activity	West Bank	Gaza Strip	Israel & Settlements	% of Total
Agriculture	15.6	14.8	7.3	14.6
Industry	14.2	11.0	16.7	13.5
Construction	8.5	9.3	46.4	12.2
Commerce	22.3	14.6	15.1	19.4
Transportation	6.3	4.7	2.9	5.5
Services & other branches	33.1	45.6	11.6	34.8
Total	100	100	100	100

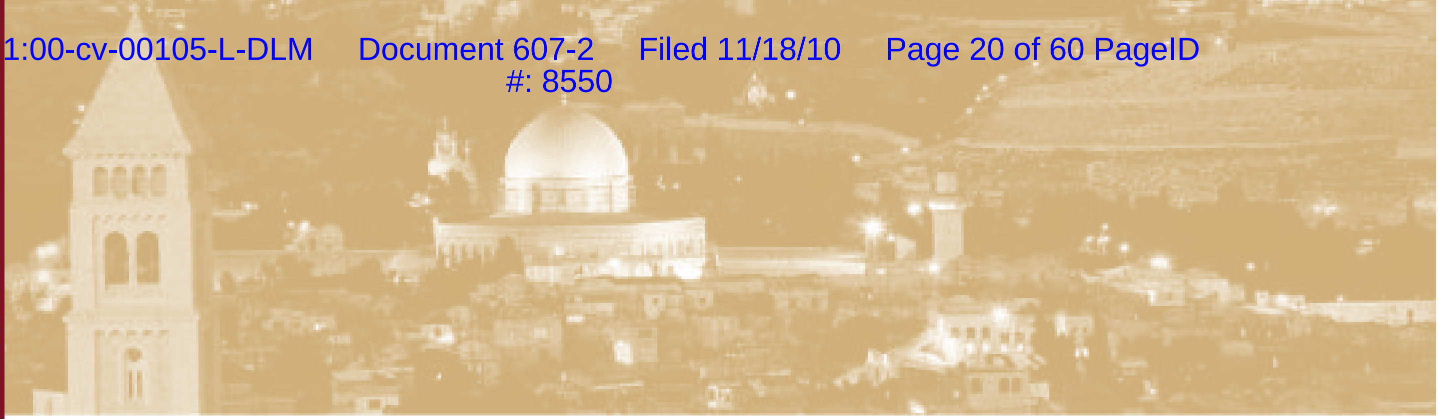
Palestinian Employed Persons in the West Bank by Economic Activity in 1st Q-2004[7]



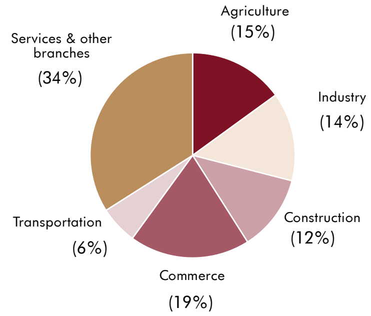
Palestinian Employed Persons in Gaza Strip by Economic Activity in 1st Q - 2004[8]



1 Palestinian Central Bureau of Statistics, Changes of Building Licenses in Remaining WBGS During 1996 to Fourth Quarter 2003.
2 Palestinian Central Bureau of Statistics, Labor Force Survey January - March 2004.
3 World Bank Report March 2004, West Bank/Gaza Update
4 Palestinian Central Bureau of Statistics, Survey on the Perception of Owners/ Managers of the Economic Establishments Towards the Economic Conditions, April 2004.
5 Palestinian Central Bureau of Statistics, Poverty Survey December 2003.
6 PCBS. Press release labor force survey results, first quarter 2004. Ramallah, Palestine. 2004.



Palestinian Employed Persons in WBGS by Economic Activity in the 1st Q - 2004[9]



The number of Palestinians employed in Israel, totaled 146,000 in the third quarter of 2000, decreased to 43,000 in the fourth quarter of 2000, and leveled off at roughly 60,000 through the end of 2003.

The remarkable increases in the number of employed persons locally reduced the unemployment rate from 31.4% at the beginning of 2003 to 20.7% by year end. In Gaza the 4th quarter 2003 unemployment rate stood at 31.9%, a slightly higher than it was at the beginning of the year.

Education

Palestinians value education highly and spend a relatively large portion of their income on education. Palestinians were only able to start developing their public education system in 1994 following the establishment of the PNA. Students in basic education (0-12 years) for the academic year 2003/2004 numbered 1,024,285 students, divided almost equally between males and females. University level students in the academic year 2002/2003 numbered 95,846, 50.6% males and 49.4% females. Enrollment in community colleges still lags behind local market demand and the levels of enrollment in neighboring countries. There are less than 7,565 students at this level, 43% male and 57% female.

Health Sector

The Palestinian health sector has fairly high costs and represents 8-10% of GDP. In absolute numbers it amounts to US $220-270 million. Approximately US $90-100 million has been spent annually through the PA budget since 1995 while the remaining cost was shared by UNRWA, donor organizations, and Palestinian non-governmental organizations (NGOs). The governmental sector provides primary health care for all Palestinians. Secondary and tertiary health care are also provided to subscribers of government insurance, delivered through nine hospitals in the West Bank and five hospitals in the Gaza Strip. Refugees receive primary health care services from UNRWA. The NGOs constitute an important group operating non-profit clinics in rural areas. The private sector is mainly involved in the provision of secondary and very limited tertiary health services in the main cities.

III. Development of Physical Infrastructure

Even prior to the Oslo Accords, Palestinian infrastructure suffered from continual under-investment (less than 1% of GDP) and very little maintenance. As a result, poor infrastructure and limited public services made the Palestinian economy the least competitive in the region. After 1994, the PNA and donors focused their efforts in this area and spent an average of US $250 million annually during 1995-2000 to develop physical and social infrastructure. The private sector was encouraged to contribute to infrastructure development and it invested in telecommunications, electricity generation, and in higher education. The following paragraphs provide brief information on the main infrastructural developments:

Road networks

The road network length islength is 4,900 km, covering an area of around 6,000 sq. km, of which 2,500 km are external roads that connect major cities with each other and with border crossings. Main roads consist mostly of two lanes with the exception of short four-lane roads around Jerusalem. The width of the main roads ranges between 4-8 m, while the width of the regional roads ranges between 3-6 m and that of local roads is 3m. The length of paved roads per 100 people is only 80m compared with 266m in Israel. Furthermore, the condition of the road network has deteriorated significantly as a result of the destruction inflicted by the Israeli military during the last three years and the PNA and donors will have to allocate considerable financial resources for road repairs and expansion.

Electricity

The Palestine Electricity Company, a private sector company, was established and publicly sold shares in 2001. Its first generation dual turbine, a 140 megawatt generation plant started operating in Gaza in 2002, ending more than 35 years of Israeli monopoly over the WBGS power supply. However, this plant is still dependent on Israeli suppliers for diesel and butane and this could affect its efficiency and competitiveness. Also, this plant is only a small step in tackling problems in the supply of electricity, which suffers from frequent disruption, weak voltage, plus high leakage and loss in the outdated network. More than 140 villages in the West Bank are still using small diesel generators. Per capita consumption of electricity is substantially below average and lower than in neighboring countries.

Water sector

Renewable Palestinian water resources are estimated at 600-750 million cubic meters per year. Palestinian use of their own water is strictly controlled by the

Israeli authorities which allocates less than 150 million cubic meters for Palestinian use and pumps most of the remainder for Israeli use. The daily per capita consumption is estimated at 90 liters, while the per capita of produced water is estimated at 145 liters daily. This fact shows the high level of leakage and loss due to the poor quality and age of the supply network.

These restrictions on the supply of water represent a violation of human and economic rights and do not take into consideration the minimum requirements for population growth, or the agricultural and industrial needs of the Palestinian people. The Israeli authorities do not allow more than one hundred villages in the West Bank access to water, forcing them to rely on springs or rain harvest wells. Furthermore, the whole of the Gaza Strip has serious water shortages and an inferior quality of supply, resulting from both seawater penetration and the exhaustion of ground aquifers.

Should the water issue be resolved on the basis of international law, Palestinians would have a surplus of water, which would result in considerable improvements in both the quantity and quality of water for household and other uses.

Telecommunications

Until the mid-nineties, the Palestinian Territories lagged behind all neighboring countries in terms of telecommunications infrastructure. In 1995, the Palestine Telecommunications Company (PALTEL) was established as a public shareholding company. PALTEL has increased the number of fixed-line telephones considerably and played a major role in preparing the Palestinian communications infrastructure for integration into global networks in accordance with international standards.

Pal-Cell was established as a limited shareholding company for mobile phones, which was expanded rapidly and was able to overcome stiff competition from Israeli companies. Over the past two years, the Israeli authorities have withheld Pall-Cell imported electronics equipment in Israeli ports and sea ports for many months, which has hampered the ability of the company to maintain or expand its services.

Airports and Seaport

The Gaza International Airport was established and became operational in 1998 after a long delay due to Israeli objections. The airport operated very limited flights to Amman, Larnaca, and Cairo but following the Intifada of September 2000, the Israeli army closed the airport, damaged the few planes owned by Palestinian Airlines, and bulldozed the airport's runway. Nevertheless, the airport could be repaired and in operation within a few months of an Israeli withdrawal and the end of restrictions on the airport.
The Israeli policy towards the establishment of the Gaza seaport was very similar. After a very long delay, the PNA started the establishment of the seaport south of Gaza City with financing from three EU member countries: France, Italy, and the Netherlands. The seaport is designed to handle large vessels of 50 to 70 thousand deadweight tons, which would enable the port to be a major trans-shipment facility. Construction work started in November 1999, with plans to conclude the first phase in 2001, but since September 2000 construction work has come to a complete halt and the Israeli authorities have not permitted work to resume.

IV. Economic Performance

The economic recovery that took place during 1998 and 1999, along with most of the economic achievements of the past decade, has actually evaporated as a result of the last three and a half years of Israeli restrictions and aggression. GNP fell from US $5.056 million in 1999 and US $5.455 million in 2000 to US $4.526 million in 2001 and US $3.768 million in 2002. The GDP followed the same trend, falling from US $4.198 million in 1999 and US $4.637 million in 2000 to US $4.034 million in 2001 and US $3.396 million in 2002. The accumulated decline in per capita GNI during 2000 to 2002 was 31% and the decline in per capita GDP was 26.8%. As a result, private consumption decreased by 6% in 2000, by 16% in 2001, and by 15% in 2002. Total fixed investments declined by 28% in 2000, 77% in 2001, and 44% in 2002.

Gross local investments increased in 1998 and 1999 to US $1,668 million and US $1,464 million respectively but declined to US $984 million in 2000, to US $209 million in 2001, and to US $119 million in 2002 as a result of the deterioration in political stability.

Private investment is heavily concentrated in construction activity. Residential construction accounted for 85 percent of total planned construction areas for the period January-September 1999. The remarkable growth in the construction sector in 2003 reported by the Palestinian Central Bureau of Statistics indicates an upturn in the growth of private investments.

Public Finance

The Palestinian budget was almost balanced during 1998-1999 but since September 2000 Palestinian revenues have declined dramatically, especially as a result of Israeli withholding Palestinian VAT and customs revenue collected by the Israeli Ministry of Finance. Furthermore, the strict siege, frequent curfews and other Israeli measures resulted in a sharp decline in domestic business activities and therefore domestic taxes and customs. The widening gap between revenues and expenditures increased from zero in the year 2000 to US $747 million in 2003, and it is estimated to reach US $872 million in 2004.

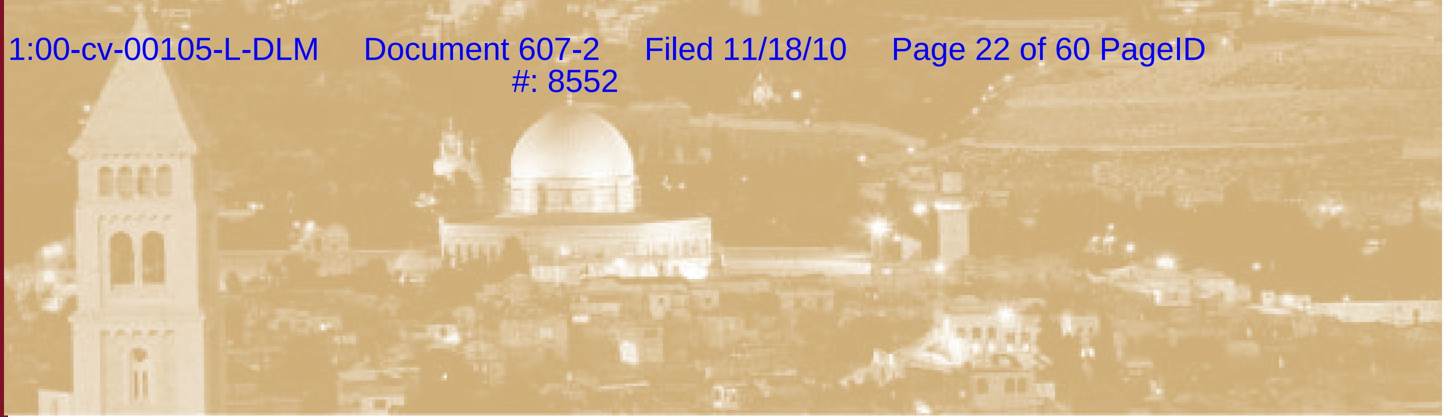
Despite the sharp decline in public revenues, the PNA was able to fulfill its obligations to its civil servants and to suppliers as well. The PNA budget actually played a remarkable role in eliminating the effects of the economic difficulties. The PNA was able to do so as a result of Arab countries and international support.

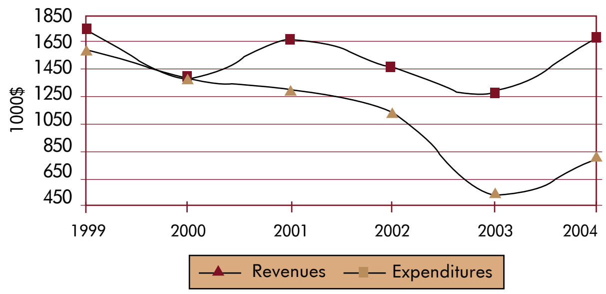
The Palestinian National Authority Budget 1999-2004[10] (in millions)

Year	1999	2000	2001	2002	2003	2004*
Revenues	1603.8	1386	1308	1133	531	806
Expenditures	1758.1	1386	1679	1476	1278	1678
Budget Deficit	154.3-	0	371-	343-	747-	872-

*** Budgeted**

7 PCBS. Press release labor force survey results, first quarter 2004. Ramallah, Palestine. 2004.
8 PCBS. Press release labor force survey results, first quarter 2004. Ramallah, Palestine. 2004.
9 Source: PCBS. Press release labor force survey results, first quarter 2004. Ramallah, Palestine. 2004.
10 Ministry of Finance, PNA Budget Law for 2004.





In addition, the PNA launched its financial reform process, which successfully improved the management and control of public revenues and expenditures. This reform not only encouraged many donors to contribute to offset the PNA budget deficit, but also resulted in better allocation and efficient use of public expenditures.

Stock Exchange

The Palestinian Stock Exchange (PSE) saw steady growth prior to 1999 but fell sharply after 2000. The value of capitalization fell from US $849 million in December 1999 to US $716 million in March 2004. The volume of trading stocks decreased from US $69 million to US $19 million in 2002, the worst year ever for the whole economy, and increased to US $40 million in 2003. The upward shift in the volume of trading in 2003 came as a result of the establishment of new Prime Minister, the quick end of the war in Iraq in April 2003, and the process of transfer and consolidation of PNA assets under the management of the Palestine Investment Fund.

V. Economic Structure

The Palestinian economy, although undergoing fairly significant diversification during 1994-2000, is still dominated by traditional sectors. The contribution of economic sectors to Palestinian GDP are as follows: agriculture employs 16% of the labor force and produces 8%; manufacturing employs 12.4% and produces 20%; the construction sector used to employ 20% of the labor force in 1998-1999 but the contribution of this sector declined to 12% in 2003; the wholesale, restaurants and hotels sector employs 20%, the services sector employs 34%; and the transportation sector employs 7%. The following paragraphs provide brief data on the most important economic sectors:

Agriculture[11]

The agricultural sector was traditionally the most significant in terms of productivity and employment but the contribution of agriculture to GDP has now dropped from 30% in 1991 to around 22% in 1995 and 10% in 1999. Employment in this sector also fell from 13% of the work force in 1995 to 12% by 2001.In 2002 and 2003 there was a significant increase in agricultural labor to 68,000, (15.3% of the total work force) but

it is uncertain if this return to agriculture will be sustained. In light of the Israeli policy of closure that rendered 140,000 workers unemployed virtually overnight, this trend may be a survival strategy rather than a strategic choice.

In 2000/2001, cultivated area covered around 1,851 thousand dunums. Most of this area, around 90%, is in the West Bank and 10% in the Gaza Strip. The Agricultural Statistics of 2001/2002 indicated that 1,181 dunums (63.8%) of the cultivated area was for fruit production, 9.4% for vegetables, and 26.8 % for field crops. Irrigated areas make up 71.5% of the total cultivated area in the Gaza Strip and 7.0% of the total cultivated area in the West Bank.

The number of livestock in 2001/2002 numbered 30,105 cows, 758,293 sheep and goats, while poultry, mainly chicken, numbered 48,909 thousand for meat production, and 2,171 thousand for egg production.

The value of agricultural output in 2000/2001 was US $856 million. Fruit and vegetables contributed 59.2% and animal production was 40.8%. More than two-thirds of agricultural output is produced in the West Bank, while the Gaza Strip produces only 28.8% of agricultural output. Gaza has a chronic shortage of animal products, especially eggs and white meat. Although the Gaza Strip produced around 2627 tons of fish in 2002, this fell short of full capacity since fishing was restricted by the Israeli authorities. The value added of agriculture was US $458 million in 2001/2002 with the West Bank contributing 64.2% and the Gaza Strip 35.8%.

The Industrial Sector

Industrial development in the West Bank and Gaza Strip was affected by Israeli policies, market conditions, and the unfavorable investment climate during the pre-Oslo period. Industry contribution to GDP remained below 10% of GDP during the 1970s and 1980s. The manufacturing structure also remained traditional. After the Oslo Accords of 1993, there were progressive changes in the industrial sector as Palestinian industrialists were able to invest, modernize their plants, and diversify industrial production free of direct Israeli restrictions. The PNA and donors assisted in improving infrastructure, including the establishment of industrial zones.

The Industrial Survey of 2002[12] showed that there were 14,179 industrial establishments, employing 65,536 persons, and their value added was US $367 million.

At the general classification, the mining and quarries branch employed 3.4% of industrial workers and produced 3.9% of industrial output with value added of 4.7%. The manufacturing sub-sector employed 94.7% of workers, its output was 88.9% and its value

added was 89.7%. The gas, electricity and water sector employed 1.9%, its output was 7.1%, and its value added was 5.7%.

Latest data on the structure of the manufacturing sub-sector indicates that the mining branch employs 3% and produces 5% of the industrial GDP, the textile and wearing apparel employs 23% of the industrial labor force, and produces 12.4% of its value added; the leather branch employs 7.8% and produce 5.4%; wood and wood products employs 3.1% and produces 2%; Chemical, plastic and rubber branches employ 4.3% of labor force and produce 7.8% of industrial GDP; non-metallic products employs 21% of industrial labor force and produces 21.7% of industrial GDP, basic metal and metallic products employs 12.5% of labor force and produces 10.6% of industrial GDP, furniture branch employs 8.9% and produces 6.8% of industrial GDP, other industrial branches employ 4.5% and produce 7.3% of the industrial GDP.

Number of Enterprises, Engaged Persons, Added Value by Industrial Branch in WBGS in 2002[13]

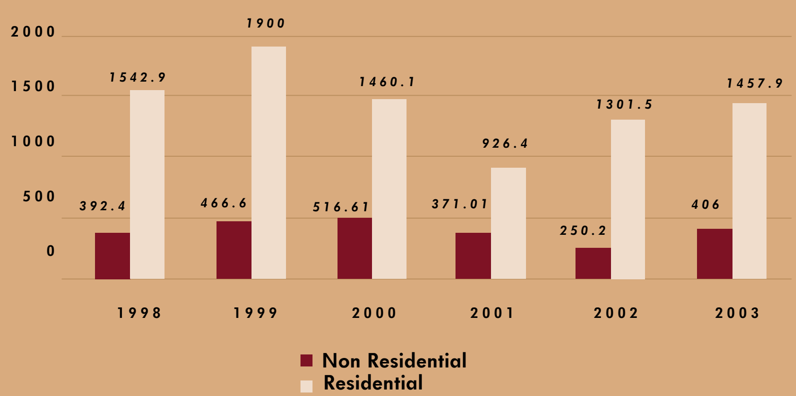
Industrial Branch	No. of Enterprises		Persons Engaged		Value Added	
	No.	%	No.	%	000 US $	%
Grand Total	14,179.00	100%	65,536.00	100%	367,050.10	100%
Other mining and quarrying	312	2%	1,998.00	3%	18,352.30	5%
Manufacture of food and beverages,tobacco products	1,661.00	12%	7,781.00	12%	76,958.50	2 1 %
Manufacture of textiles, wearing apparel	2,183.00	15%	15,052.00	23%	45,633.50	1 2 %
"Tanning of leather; manufacture of bags"	782	6%	5,141.00	8%	19,852.30	5%
Manufacture of wood and its products	796	6%	2,039.00	3%	7,249.60	2%
Manufacture of chemicals & its products, rubber and plastic	337	2%	2,831.00	4%	28,619.60	8%
Manufacture of non-metallic products	1,917.00	14%	13,747.00	21%	79,640.30	2 2 %
Manufacture of basic metals, metal products, machinery and equipment	3,335.00	24%	8,220.00	13%	38,891.70	1 1 %
Manufacture of furniture	2,126.00	15%	5,810.00	9%	25,018.10	7%
others	793	6%	2,917.00	4%	26,834.20	7%

The Construction Sector

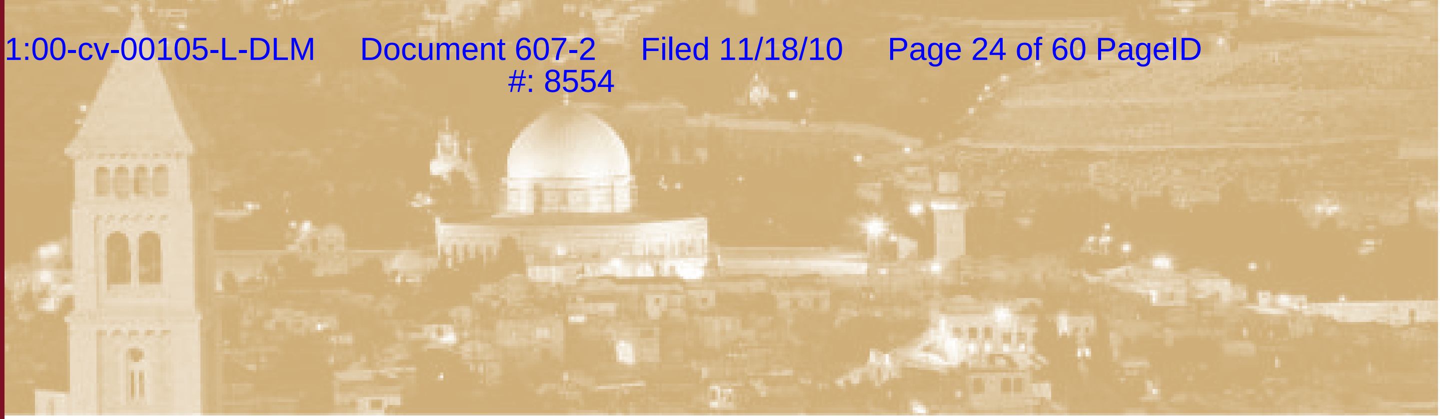
The construction sector was significantly affected by Israeli restrictions on land use and the minimal investment in infrastructure. After a long period of stagnation from the early 1980s to early 1990s, this sector grew rapidly following the Oslo Accords in 1993. The area of building under construction increased from a few hundred thousand square meters in the 1980s to more than 2.5 million square meters annually during 1993 to 2000. The area of building starts declined from 2.457 million square meters in 2000 to 1.633 square meters in 2001, and declined further to 1.080 square meters in 2002. In 2003, the area of building starts witnessed a considerable increase to 1.863 square meters. This growth could be seen also in other indicators such as the number of buildings and building licenses issued.

The considerable growth cited in the construction sector represents a strong signal of economic recovery. This sector historically absorbs more than 80% of private investment. Furthermore, the construction sector has very rich backward and forward linkages in the economy. Thus its growth will stimulate growth in other sectors. But the sustainability of this growth will remain dependent on political stability.

New building lincens in the WBGS in 2003



11 All data on agriculture are based on the Agricultural Statistics 2001/2002, PCBS, August 2003.
12 PCBS, Industrial Survey 2002, unpublished data, 2004.
13 Palestinian Central Bureau of Statistics, 2004. (Unpublished Data)



Tourism

The tourism sector has great potential due to the fact that Palestine is the birthplace of three religions, many historical and archeological sites and a mild climate. However, tourism is the most sensitive sector to political instability and as a result, this sector's contribution to GDP was insignificant prior to the Oslo Accords in 1993. After that, the tourism sector rocketed, particularly on the eve of the millennium year, 2000. Investment in new hotels, restaurants, car rental, tourist coaches, antiquity and gift shops, leisure facilities and other services was very high.

The number of hotels grew from around 30 concentrated in Jerusalem and Bethlehem to 75 hotels distributed in all the main Palestinian cites. By 2002, the number of operating hotelsoperating hotels had fallen by 21% compared with 1999. The number of hotel rooms increased from under 1000 with around 2000 beds to 3052 rooms with 6598 beds. For the first time, international chains such as the Intercontinental joined Palestinian investors and built state- of-the-art new hotels.

By the end of 2002, there were 266 employees in hotel management and 935 additional workers. These numbers were 26% less than in 1999 and hotel occupancy decreased dramatically due to the deterioration in the political situation. Occupancy declined by 5% in 2000, by 74% in 2001, and by 81% in 2002 compared with 1999. The total number of visitors in 2002 was less than 170,000, with 40% of them local Palestinians. The data of the fourth quarter of 2003 indicate a slight growth in the occupancy rate to 8.2%.

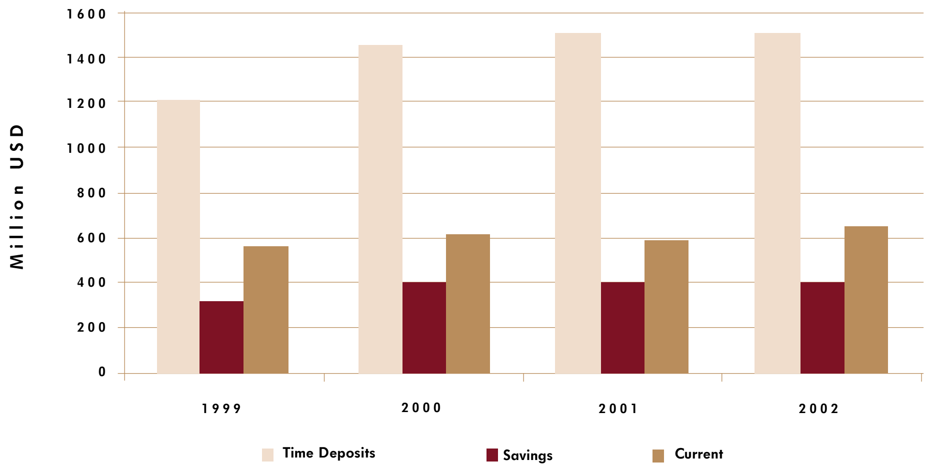
The sharp decline in the number of tourists impacted other related businesses such as restaurants, shops and transportation and many companies in the tourism sector have ceased operations.

Nevertheless, tourism remains one of the most promising sectors and has the potential to be a major job generation factor in the Palestinian economy if political conditions improve.

The Financial Sector

The financial sector witnessed unprecedented growth in both the banking and insurance sectors. The number of banks increased from two banks with 13 branches in 1993 to 21 banks with 120 branches in 2003. Private deposits have grown from less than US $150 million prior to 1993 to US $1501 million in December 1996 and to US $3.506 billion in September 2000. Since then, there has been a slight decline due to the deterioration in the political situation and private deposits totaled US $3.4 billion in June 2002.

Time Deposits, Savings, Currents at the Ends of Year 1999-2002



Bank credit to the private sector witnessed steady but slow growth from 1994 to September 2000 but growth then slowed as a result of the deterioration in the investment climate and in all aspects of economic activity. Credit grew from US $1005.5 million in 1999 to US $1346 million in 2000, but then started a gradual decline to US $1221 million in 2001 and US $950 million in 2002. In 2003, bank credit resumed an upward trend and grew to US $970 million by June 2003.
Credit extended to the private sector was predominantly overdraft facilities with one year or less maturity (55%), term loans with 3 years or less maturity (45%) and under 3% discounted bills. The Palestinian economy lacks the provision of long term credit to finance investment.

The number of insurance companies rose from one to nine. Four of these are new Palestinian companies, two Arab, and the others are foreign companies which opened branches in the WBGS. These companies now employ 718 employees and their added value was US $15 million.

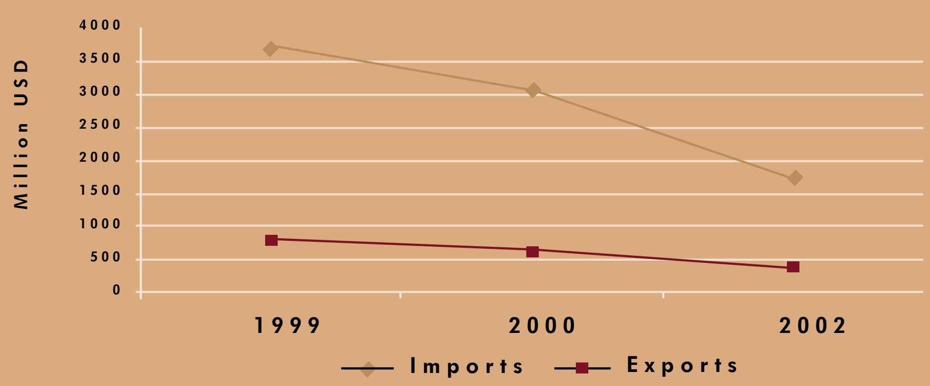
The Information Technology Sector

One of encouraging features of the Palestinian economy is the emergence of the information technology sector. This sector grew strongly during the last ten years, and especially after the privatization and development of the telecommunications sector. The number of IT companies increased from 25 in 1994 to 61 in 2000. They are mainly concentrated in software application production, data processing, and in the sale and maintenance of hardware. Very few are engaged in research and hardware development in cooperation with international companies.
This sector employs several hundred highly-skilled and highly paid employees but its contribution to GDP remains insignificant. The capacity of these software development companies exceeds local demand and they have started to look at promising Arab markets, especially the Gulf statesStates and Saudi Arabia. Since 2000, these companies exhibit at many international IT exhibitions such as COMDEX and GITEX. Furthermore, they have opened a marketing office in Dubai.
The potential of the IT sector will be very much improved by the new initiatives aimed at developing IT human resources in Palestinian universities and professional IT training centers.

Foreign Trade

The volume and value of Palestinian foreign trade fell by almost 50% from 1999 to 2002. Palestinian merchandise exports decreased from US $763 million in 1999 to US $353 million in 2002. Imports also decreased from US $3712 million to US $1737 million for the same period. The recent data of the year 2003 indicate further deterioration. Imports from Israel decreased in the third quarter of 2003 to US $331 million, which is 24.6% less than in the third quarter of 2000. Exports to Israel also witnessed a sharp decline to US $50 million, which is 28.8% less than the third quarter of 2000. This level of decline reflects the overall deterioration in the export sectors in the economy.
Palestinian foreign trade remains stunted not only by Israeli trade policy, but also by restrictive Israeli procedures and policies with regard to ground, sea and air transportation. Impediments to trade unfortunately deprived the Palestinian private sector of the ability to benefit from free trade agreements with the European Union, the United States, Canada, and some Arab countries. Palestinian goods are still mainly destined for the Israeli market, which absorbs more than 90% of exports and is the source of more than 85% of Palestinian imports.

Foreign Trade Through the Period 1999-2002



Foreign Trade Commodity Structure

The commodity structure of Palestinian trade prior to September 2000 indicates that manufactured goods are the largest category of exports with a 42 percent share of the total value of exports. Food and live animals occupied the second largest category of exports (16%), followed by miscellaneous manufactured articles (15.6%), beverages and tobacco, together with chemicals and related products (6% each) and raw materials (4%). Exports of vegetables and fruit totaled US $35 million and represented 8% of total exports, followed by furniture (US $24 million), iron and steel (US $18 million) and footwear (US $19 million). Meanwhile, stone and marble continue to be the single most significant Palestinian export, worth over US $100 million.
Manufactured goods ranked as the largest category of imports (23 %), followed by food and live animals (19 %), mineral fuels lubricants (17 %), and machinery and transport equipment (16 %). Other major import items include miscellaneous manufactured goods (7%), chemicals and related products (6 %), and beverages and tobacco (4 %).

BOD COMMITTEES

Auditing Committee	*Conflicts Committee*	*Investment Committee*	*Nomination Committee*
Dr. Salam Fayyad **Chairman**	**Talal Nasiruddin** **Chairman**	**Maher Masri** **Chairman**	**Sabih Masri** **Chairman**
Jawdat Khoudary **Member**	**Mohamed Rachid** **Member**	**Talal Nasiruddin** **Member**	**Samer Khoury** **Member**
Samer Khoury **Member**	**Jawdat Khoudary** **Member**	**Sabih Masri** **Member**	**Talal Nasiruddin** **Member**
Mohamed Rachid **Member**		**Jawdat Khoudary** **Member**	**Jawdat Khoudary** **Member**
		Mohamed Rachid **Member**	**Mohamed Rachid** **Member**

STATEMENT OF COMMITTEE RESPONSIBILITIES

Audit Committee

- Oversees and monitors all aspects of the PIF's accounting and financial reporting processes.
- Takes any actions as it may deem desirable or appropriate to provide for the reliability and credibility of the PIF's financial statements and the integrity of the PIF's financial reporting process.
- Has the authority and responsibility t select, evaluate and replace the independent auditors.
- Discusses with the Accountants the overall scope and plans for their audits including the adequacy of staffing and compensation.
- Reviews with management and the Accountants the PIF's annual and interim financial statements.

Conflicts Committee

- Consults with the Board of Directors in the event of conflicts of interest, and acts thereon as provided under the Articles of Incorporation.
- Reviews general economic and financial trends.
- Reviews all portfolio investments.
- Reviews and prepares a report to the Board of Directors concerning any proposed Portfolio Investment in which the General Manager, any other officer of the PIF or any Director shall have an interest.

Investment Committee

- Reviews all Portfolio Companies proposed for investment by the PIF.
- Supervises, receives and considers the reports of the Persons conducting transparency diagnostic reviews of proposed PIF investments.
- Subject to the Investment Guidelines, approves the investments by the PIF and the terms and conditions of any such investment.

Nominating Committee

- Nominates Persons to fill Board of Directors vacancies.

2003 Audited Finanacial Statements

Auditor's Report

To The Shareholders Of
Palestine Investment Fund Company
Gaza - Palestine

We have audited the accompanying consolidated balance sheet of PALESTINE INVESTMENT FUND COMPANY (PIF) as of December 31, 2003 and the related consolidated statements of income, changes in shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the company's Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Palestine Commercial Services Company (PCSC), Palestine Technology and Educational Complex (American school) and the Tri Fitness Company as of December 31, 2003, whose total assets equal 5.2% while its operating revenue equals 51.6% of the Palestine Investment Fund Consolidated Financial Statements as of December 31, 2003 were audited by other auditors. Saba & Co. issued their unqualified opinion on the financial statements of Palestine Commercial Services Company and Palestine Technology and Educational Complex (American School), while Talal Abu-Ghazaleh & Co. issued their unqualified opinion on the financial statements of Tri Fitness Company.

We conducted our audit in accordance with International Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion based on our audit and the reports of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PALESTINE INVESTMENT FUND COMPANY as of December 31, 2003, the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PIF is contingently liable for costs associated with winding down the operations of some investments that were transferred by the Palestinian National Authority to Palestine Investment Fund. The amount of liability, if any, is not quantifiable and therefore was not provided for in the attached financial statements.

Amman - Jordan
April 3, 2004

Ernst + Young

CONSOLIDATED
Balance Sheet
As of December 31, 2003
(In U S Dollars)

	Notes	(In U S Dollars)
ASSETS		
Cash on hand and at banks	3	43,787,006
Accounts Receivable	4	38,423,893
Due from Palestinian National Authority		4,573,792
Available for sale investments	5	272,739,480
Investments in associates		237,643,854
Loans originated by the fund	6	35,325,000
Investment properties	7	19,403,570
Projects in process		31,180,009
Other assets	8	8,973,535
Fixed assets, net	9	55,669,653
Goodwill, net	10	**51,711,502**
Total Assets		**799,431,294**
LIABILITIES AND SHAREHOLDERS - EQUITY		
LIABILITIES -		
Due to banks	11	8,857,091
Accounts payable		15,748,443
Other liabilities	12	23,797,732
Short term loans	13	17,642,714
Current portion of lease obligations	14	**1,225,710**
Total Current Liabilities		67,271,690
Long-term lease obligations	14	**19,396,071**
Total Liabilities		**86,667,761**
SHAREHOLDERS EQUITY	15	
Issued Capital		500,000,000
Advance on capital increase		71,740,227
Statutory reserve		4,012,864
Proposed dividend		35,000,000
Translation adjustment		1,408,529
Net unrealised gains on available for		
sale investments	16	16 99,486,139
Retained Earnings		**1,115,774**
Total Shareholders Equity		**712,763,533**
Total liabilities and Shareholders Equity		**799,431,294**

The accompanying notes from 1 to 27 are an integral part of these financial statements

CONSOLIDATED

Income Statement

For the year Ended on December 31, 2003
(In U S Dollars)

	Notes	(In U S Dollars)
REVENUES		
Operating Revenues, net	17	7,849,333
Income from sale of investment		19,391,328
Dividend income		2,165,526
Interest income		5,039,866
Income from associates		30,492,688
Currency difference of exchange		**20,129,387**
Total Income		**85,068,128**
EXPENSES		
General and administrative expenses	18	-11,070,659
Depreciation and amortization expenses		-18,786,068
Interest expenses		-2,745,158
Assets written off		-1,936,520
Other expenses, net		**-2,413,838**
Total Expenses before provisions		**-36,952,243**
Provision for assets? impairment		-1,930,000
Provision for doubtful accounts and advances		-4,057,247
Other provisions		**-2,000,000**
Net Income		**40,128,638**
		US$
Earnings per share		**0.07**
		No. of shares
Weighted average number of shares		**574,140,227**

The accompanying notes from 1 to 27 are an integral part of these financial statements

CONSOLIDATED STATEMENT OF CHANGES IN

Shareholders' Equity

For the year ended Decemper 31, 2003
(In US Dollars)

	Issued Capital	Advances on capital increase	Statutory reserve	Proposed dividends	Translation adjustment	Net unrealised gains on available for sale investments	Retained Earnings	Total
Balance as of 1 Janyary 2003	_	_	_	_	_	_	_	_
Issue of share capital	500,000,000	71,740,227	_	_	_	_		571,740,227
Net profit	_	_	_	_	_	_	40,128,638	40,128,638
Appropriation	_	_	4,012,864	_	_	_	-4,012,864	_
Net unrealised gains on available for sale investments	_	_	_	_	_	99,486,139	_	99,486,139
Translation Adjustment	_	_	_	_	1,408,529	_	_	1,408,529
Proposed dividend	_	_	_	35,000,000	_	_	-35,000,000	_
Balance as of 31 Dec-03	**500,000,000**	**71,740,227**	**4,012,864**	**35,000,000**	**1,408,529**	**99,486,139**	**1,115,774**	**712,763,533**

The accompanying notes from 1 to 27 are an integral part of these financial statements

CONSOLIDATED

Cash Flows

For Ther Year Ended On December 31, 2003
(In Us Dollars)

	DECEMBER 31, 2003 (In U S Dollars)
CASH FLOWS FROM OPERATING ACTIVITIES	
Net Income	40,128,638
Adjustments for -	
Net finance cost	-2,294,708
Income from associate	-30,492,688
Gain from foreign currency revaluation	-20,087,295
Dividend income	-2,165,526
Depreciation and amortization	18,786,068
Gain on disposal of available-for-sale investments	-19,391,328
Assets impairment losses	1,930,000
General provision	6,057,247
Operating profit before working capital changes	-7,529,592
Increase in accounts receivable	-35,394,907
Deposit - Palestinian Ministry of Finance	-35,814,290
Increase in other assets	-5,897,321
Increase in accounts payable	9,848,443
Increase in other liabilities	-10,491,623
Cash used in operations	-85,279,290
Interest paid	-2,455,802
Net cash flows used in operating activities	**-87,735,092**
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of property, plant and equipment, net	-390,584
Purchase of investment property	-6,198,114
Purchases of available-for-sale financial assets	-5,976,497
Payments on projects in progress	-10,910,009
Proceeds from sale of available-for-sale financial assets	123,332,029
Loans originated by the fund	-35,325,000
Investments in associate	-37,265,750
Dividend income	2,165,526
Interest received	1,963,652
Net cash flows from investing activities	**31,395,253**
CASH FLOWS FROM FINANCING ACTIVITIES	
Payment of finance lease obligations	-1,284,410
Repayment of loan	-24,666,506
Proceed from overdraft facility	900,553
Proceed form short-term borrowing	14,000,000
Net cash flows used in financing activities	**-11,050,363**
Net decrease in cash	**-67,390,202**
Cash and cash equivalent, beginning balance	73,954,389
Net foreign exchange difference	1,408,529
Cash and cash equivalent, as of December 31, 2003	**7,972,716**

The accompanying notes from 1 to 27 are an integral part of these financial statements

NOTES TO THE

Consolidated Financial Statements

As Of December 31, 2003
(In U S Dollars)

(1) GENERAL

Palestine Investment Fund Company (PIF), a Public Shareholding Company, was incorporated in Gaza under number 56200718, on March 17, 2003 with a share capital of US$ 500,000,000. The sole shareholder of the company is the Palestinian National Authority.

The company was established as a successor to the Palestinian National Authority investment practices, as a result of the decree issued by the President of the Palestinian National Authority on October 1, 2000, which stipulated the transfer of all Palestinian National Authority investments to the Palestine Investment Fund. The fair market value of the investments was designated as the Palestinian National Authority share in the new Company's capital. The company commenced its' operations on January 1, 2003.

Palestine Investment Fund Company (PIF) aims to acquire/invest, and to sell/dispose off all types of investments that promote economic growth and infrastructure development in Palestine. PIF also seeks to stimulate private sector investment, both domestic and foreign, to achieve sustainable long-term economic prosperity for Palestine.

A substantial portion of the Palestine Investment Fund assets and liabilities (including cash balances, investments, loans originated by the fund and term loans) are still registered in Palestine Commercial Services Company name.

The number of employees in the Fund and its' subsidiaries as of December 31, 2003 was 223 employees.

The Financial Statements were approved by the Board of Directors in their meeting held on April 3, 2004.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards, as published by the International Accounting Standards Board and interpretations issued by International Financial Reporting Interpretations Committee under the historical cost convention except for available for sale investments, which are stated at their fair values.

The consolidated financial statements comprise the financial statement of Palestine Investment Fund and its fully owned subsidiaries, Palestine Commercial Services Company (PCSC), American School and Tri Fitness Company. The subsidiary is consolidated from the date on which control is transferred to the Fund and ceases to be consolidated from the date on which control is transferred out of the Fund.

The financial statements of the Fund and its subsidiary for the same financial period are prepared using the same accounting policies.

Following is a summary of significant accounting policies:

2.1 Cash and cash equivalents -

Cash includes cash on hand and cash at banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

2.2 Available for sale investment -

The investments are classified, in accordance with the IAS 39 Financial Instruments: Recognition and Measurement, into the following categories: held to maturity, trading and available-for-sale. Investments with fixed or determinable payments and fixed†maturity that the Fund has the positive intent and ability to hold to maturity are classified as held to maturity investments. Investments acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as trading. All other investments are classified as available for sale.

All purchases and sales of investments are recognized on the trade date.

Investments are initially measured at cost, which is the fair value of the consideration given for acquiring the investment, including transaction costs.

Available for sale and trading investments are subsequently carried at fair value without any deduction for transaction costs by reference to their quoted market price at the balance sheet date.

Gains or losses on measurement to the fair market value of available for sale investments are recognized directly in the " Net unrealized gains on available-for-sale investment" in the shareholders' equity.

2.3 Investments in associates -

The Fund's investments in associates are accounted for under the equity method of accounting. These are entities in which the Fund has between 20% to 50% of the voting power or over which it exercises significant influence. Investments in associates are carried in the balance sheet at cost, plus post-acquisition changes in the company's share of net assets of the associate, less any impairment in value. The income statement reflects the Fund's share of the results of its associates.

2.4 Investment in real estate -

Buildings are stated at cost less accumulated depreciation and impairment provision. Buildings are depreciated using the straight line method at an annual rate of 5%.

Investment in land is stated at fair market value reported by Standard and Poor's as of January 1, 2003.

2.5 Goodwill -

Goodwill represents the excess of the fair value assigned to the net tangible assets of businesses acquired over PIF share in the shareholder's equity. Goodwill is amortized on a straight line basis over 5 years. Periodically, the Fund reviews the recoverability of good will. The measurement of possible impairment is based primarily on the ability to recover the balance of the goodwill from expected future operating cash flows on an undiscounted basis. It is management's opinion that no material impairment exist at December 31, 2003.

2.6 Fixed assets -

Fixed assets are stated at cost less accumulated depreciation and accumulated impairment loss. When assets are sold or retired, their cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposal is included in the income statement.

Fixed assets are depreciated over the estimated useful lives using straight - line method with annual rates ranging from 7% to 50%.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use.

2.7 Leases -

Finance leases, which transfer to the Fund substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

2.8 Translation of the financial statements of foreign subsidiaries -

The financial statement of subsidiaries where the local currency is the functional currency are translated into U.S Dollars using exchange rates in effect at period end for assets and liabilities and average exchange rates during each reporting period for results of operations. Adjustments resulting from translation of financial statements are reflected as a separate component of shareholders' equity.

2.9 Revenue recognition -

2.9.1 Sales are recognized when the significant risks and rewards of ownership of the goods have passed to the buyer and the amount of revenue can be measured reliably.

2.9.2 Investment revenue is recognized for the difference between the book value and the selling price on the transaction date. The re-evaluations of the investments are recorded according to the investment policy mentioned in 2.2 above. The revenues from associated companies are recorded according to the investment policy mentioned in 2.3 above.

2.9.3 Interest revenue is recognized as the interest accrues.

2.9.4 Dividends revenue is recognized when the shareholders' right to receive the payment is established.

2.10 Provision -

Provision are recognized when the Fund has a present obligation (legal or constructive as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

2.11 Foreign currency -

Assets and liabilities denominated in foreign currencies are translated to United States Dollars using the prevailing exchange rates at year-end. Foreign currency transactions during the year are recorded using exchange rates that were in effect at the dates of the transactions. Foreign exchange gains or losses are reflected in the statement of income

(3) CASH ON HAND AND AT BANKS

This item consists of the following:

Cash on hand	687,889
Cash at banks	7,284,827
Deposits *	35,814,290
	43,787,006

* This amount represents a deposit placed under the name of the Palestinian Ministry of Finance. This amount is restricted and not available for use.

(4) ACCOUNTS RECEIVABLE

This item consists of the following:

Orascom Telecommunication Holdings	7,240,801
Palestine Telecommunication Company	15,087,352
Palestine Pension Fund	4,951,092
Orascom Telecommunication Tunisie S.A.	2,738,264
Alberta Ltd.	1,087,571
Checks under collection	2,378,389
Cement trading receivable	4,708,699
Students receivable	209,289
Others	717,124
	39,118,581
Provision for doubtful debts	-694,688
	38,423,893

(5) AVAILABLE FOR SALE INVESTMENTS

This item consists of the following:

Investments in companies with quoted shares	152,386,969
Investments in companies with unquoted shares	85,125,020
Portfolios investments	35,227,491
	272,739,480

(6) LOANS ORIGINATED BY THE FUND

This item consists of the following:

Orascom Telecom Company	35,000,000
Arab Paper Hygienic Product Company	325,000
	35,325,000

Orascom Telecom Holding Company -
Palestine Commercial Services Company granted Orascom Telecom Holding Company a loan of USD 35,000,000 on December 11,2002 bearing an interest rate of libor + 3% per annum which was subsequently amended to a fixed rate of 8% per annum with a maturity date of July 31, 2004.

The Arab Paper Hygienic Product Company (Carmen)-
Palestine Investment Fund granted Arab Paper Hygienic Product Company a loan of USD 325,000 on September 2, 2003 bearing an interest rate of 10% with a maturity date of March 1, 2004.

(7) INVESTMENT PROPERTIES

This item consists of the following:

Investments in lands	11,670,602
Investments buildings	7,813,750
	19,484,352
Less: Accumulated depreciation	-80,782
	19,403,570

(8) OTHER ASSETS

This item consists of the following:

Accrued interest income	3,076,214
Cash margin against letter of credit	2,800,000
Advances to suppliers	1,859,823
Value added taxes	935,342
Employees receivables	935,203
Prepaid expenses	438,887
Inventory	150,169
Refundable deposits	58,535
Others	511,362
	10,765,535
Less: Provision for uncollectable advances	-1,792,000
	8,973,535

(9) FIXED ASSET
This item consists of the following:

	Land **	Buildings	Aircrafts *	Aircraft Components	Vehicles	Equipment, machinery and computer	Furniture, fixture and decoration	Projects in progress (Tri fitness)	Total
Cost -									
January 1, 2003	1,611,019	7,303,441	_	_	895,227	1,390,878	918,216	1,677,740	13,796,521
Additions	_	_	49,000,000	322,000	57,000	73,761	168,357	1,063,014	50,684,132
Retirements	481,983	249,641	_	_	82,855	_	279,528	_	1,094,007
At December 31, 2003	**1,129,036**	**7,053,800**	**49,000,000**	**322,000**	**869,372**	**1,464,639**	**807,045**	**2,740,754**	**63,386,646**
Accumulated Depreciation -									
January 1, 2003	_	807,484	_	_	608,293	493,994	152,270	_	2,062,041
Additions	_	241,443	4,900,000	32,300	97,971	266,511	239,186	_	5,777,411
Retirements	_	_	_	_	44,141	_	78,318	_	122,459
At December 31, 2003	_	**1,048,927**	**4,900,000**	**32,300**	**662,123**	**760,505**	**313,138**	_	**7,716,993**
Net carrying amount	**1,129,036**	**6,004,873**	**44,100,000**	**289,700**	**207,249**	**704,134**	**493,907**	**2,740,754**	**55,669,653**

* Two Dash-8 aircraft with a cost of USD 19,500,000 are registered under the name of the Palestinian Airlines, for which the Fund had obtained a Trust Deed for the ownership of these aircraft.
** Tri-fitness land with a cost of USD 993,278 is not registered in the company's name.

(10) GOODWILL, NETS

In connection with the Palestinian National Authority contribution to the Palestine Investment Fund capital, the excess of the fair market value of the investment in associates and subsidiaries over PIF ownership share in the shareholders equity of the company were reported as goodwill. The goodwill is being amortized using the straight line method over 5 years.

Goodwill	64,639,377
Goodwill Amortization	-12,927,875
	51,711,502

(11) DUE TO BANKS

This item represents the utilized amount from the credit facilities obtained by the Palestine Commercial Services Company from Palestine Investment Bank with a ceiling of US $ 8,000,000 at an interest rate of 5%.
The facility was guaranteed by pledging 2,112,000 shares of PADICO and 550,000 shares of Palestine Telecom Company.

(12) OTHER LIABILITIES

This item consists of the following

End of service benefits	1,415,819
Unearned interest	2,074,525
Accrued expenses	927,256
Accrued interest expense	289,355
Contractors retention	69,183
Other reserves	2,000,000
Due to PNA from prior year income	17,000,000
Others	21,594
	23,797,732

(13) SHORT TERM LOAN

This item consists of the following:

Arab bank loan *	3,642,714
Cairo Amman bank **	14,000,000
	17,642,714

* On June 18, 2000, Palestine Commercial Services Company was granted a loan amounting to 13,600,000 US Dollars. The loan is subject to an annual interest rate of Libor plus 1.5 per annum. The principle and the interest were payable on October 18, 2000.
The loan was rescheduled during December 2000, to amend the settlement of the loan to 12 monthly instalmentsof USD 1,000,000 the first of which was due on January 1, 2001 and the last on December 31, 2001. The loanwas due but is not paid till the date of the financial statement.
The loan was guaranteed by pledging 1,500,000 shares of Palestine Telecommunication Company and 6,177,000 shares of PADICO.

** On December 4, 2003, the Fund was granted a loan amounting to US$14,000,000 The loan is subject to an annual interest rate of LIBOR plus 2% with a minimum interest rate of 3% which is payable quarterly. The loan is payable within one year from the agreement date.
The loan was guaranteed by pledging 3,000,000 GDR shares of Orascom Telecom Holding Company, 1.89 million shares in Palestine Telecom Company and the Amount due from Palestine Telecom Company related to Palcel shares sale amounting to USD 14,000,000.

(14) LEASE OBLIGATION

This item consists of the following:

	Challenger 604	Lear jet 60	Total
Short term obligations	611,287	614,423	1,225,710
Long term obligations	14,835,714	4,560,357	19,396,071
	15,447,001	5,174,780	20,621,781

Challenger 604 lease agreement

The lease agreement was signed on October 8,2002. The term of the agreement is for seven years. Interest on the lease is computed based on LIBOR plus 3.35% with a minimum interest rate of 5.35%.

The lease is guaranteed by retaining the ownership of the aircraft until Leasee perform all the obligations under the lease agreement, in addition to a letter of credit amounted to US$ 1,500,000.

Learjet model 60 lease agreement

The lease agreement was signed on March 22, 2002. The term of the agreement is for seven years. Interest on the lease is computed based on LIBOR plus 3.51%, with a minimum interest rate of 5.51%.

The lease is guaranteed by promissory note amounted to USD 6,120,000 together with interest due on the loan.

(15) SHARE HOLDERS EQUITY

- Issued Capital

The issued capital of the Fund consists of all assets and liabilities transferred from the Palestinian National Authority to the company, valued at their estimated fair market value as of January 1, 2003, as issued and determined by Standard and Poor's.

The details of the Palestinian National Authority (PNA) capital contribution is as follows:

Fair Market Value of investments contributed by the PNA	574,148,734
Cash balances contributed and retained by the PNA	73,954,389
	648,103,123
Liabilities and commitments	-44,362,896
Net assets contributed by the PNA	603,740,227
Due to PNA for prior years' income	-32,000,000
	571,740,227

The net fair value of the assets and liabilities contributed to Palestine Investment Fund were allocated to the capital and advance on capital increase.

- Advance on capital increase

The advance on capital increase represents the difference between the registered and issued capital and the total fair market value (excluding associated liabilities) of the contribution made by the Palestinian National Authority to the Fund capital.

- Statutory reserve

This amount represents the appropriations at 10% of net income. This reserve is not available for distribution to shareholders.

- Voluntary reserve

The amount represents the appropriations not exceeding 20% of net income. This reserve is available for distribution to shareholders.

- Proposed dividend

The Board of Directors resoluted to distribute USD 35,000,000 as dividends, in accordance to the Palestinian Legistlative resolution.

(16)UNREALIZED GAINS ON AVAILABLE FOR SALE INVESTMENTS

This amount includes an unrealized revaluation gain of the Fund's investment in Orascom Telecommunication Holding Company shares of USD 95,617,600.

(17) OPERATING REVENUE, NET

This item consists of the following:

	Revenue	Cost	Net Revenue (loss)
Aviation operations	2,392,154	2,890,796	-498,642
Cement operations	62,604,128	53,169,375	9,434,753
School operations	564,286	1,606,549	-1,042,263
Tri Fitness center operations	221,431	265,946	-44,515
	65,781,999	57,932,666	7,849,333

(18) GENERAL AND ADMINISTRATION EXPENSES

This item consists of the following:

Salaries and wages	3,228,208
Bonuses and benefits	257,927
Travel expenses	1,017,379
Professional fees	2,943,773
Insurance expenses	112,209
Maintenance expenses	57,996
Rent	298,255
Ramalla office expenses	538,046
Hospitality and hotels	213,139
Printing and stationary	37,094
Membership, subscriptions fees and commission	451,211
Donations	991,333
General expenses on projects	57,349
Post and telephones	244,620
Board of Directors expenses	51,800
Others	570,320
	11,070,659

(19) CASH AND CASH EQUIVALENT

Cash and cash equivalent that appears in the cash flow statements consist of amounts that appear in the balance sheet and are as follows:

Cash on hand and at banks	43,787,006
Less: Deposits - Ministry of Finance	35,814,290
	7,972,716

20) RISK MANAGEMENT

Interest rate risk

The fund is exposed to interest rate risk on its interest bearing assets and liabilities (bank deposits, loans originated by the fund, due to, banks, lease obligations and term loan).

Credit risk

The fund maintains its bank accounts and deposits in reputable financial institutions.

The fund seeks to limit its credit risk with respect to customers by setting credit limits for individual customers and monitoring outstanding receivables.

Liquidity risk

The fund limits its liquidity risk by ensuring bank facilities are available. The fund's terms of sales require amounts to be paid within 30 days of the date of sale. Trade payables are normally settled within a reasonable days of the date of purchase.

Currency risk

Most of the transactions are dominated in United State Dollars, except for investments held in Tunisia, Algeria and Palestine.

(21) FAIR VALUES OF FINANCIAL INSTRUMENTS

Financial instruments comprise of financial assets and financial liabilities.

Financial assets consist of cash and bank balance, receivables investments and other assets, financial liabilities consist of bank overdrafts, term loans, obligations under finance leases, payables, and accrued expenses.

The fair values of financial instruments are not materially different from their carrying values.

(22) INVESTMENTS IN SUBSIDIARIES

The consolidated financial statements include the financial statements of Palestine Investment Fund and the subsidiaries listed in the following table.

Name	Country of incorporating	Ownership	Fair Market Value
Palestine Commercial Services Company	Palestine	100%	54,000,000
Palestine Technology and Educational			
Complex (American School)	Palestine	100%	2,900.00
Hanadi Tower	Palestine	100%	5,000,000
Tri Fitness Company	Palestine	100%	3,000,000
Fair value of net assets			64,900,000
Goodwill arising from PNA capital contribution			-43,297,496
			21,602,504

(22) INVESTMENT IN ASSOCIATES

Palestine Investment Fund investments in associates are as follows:

Name	Country	Ownership	Fair Market Value Jan. 1, 2003
Cap Holdings Oasis Hotel Casino Resort	Palestine	23.08%	28,510,000
Palestine Tourism Investment Company	Palestine	22.05%	2,000,000
Engineering Technicians Company for			
Contracting and Maintenance	Palestine	45%	230,000
Grand Park Hotel & Resorts	Palestine	25.78%	100,000
Al-Ahlia Trading and Industrial Services			
Company	Jordan	45%	300,000
Orascom Telecommunication Tunisie S.A. *	Tunis	22.03%	50,000,000
Orascom Telecommunication Algerie Spa *	Algeria	25.29%	90,000,000
Fair value of net assets			171,140,000
Goodwill arising from PNA capital contribution			-21,341,881
			149,798,119

* Palestine Investment Fund has an indirect ownership in those two companies through its direct ownership in Orascom Tunisia Holding Ltd. BVI, Cathage Consortium Ltd. (Tunis) and its direct ownership in Oratel International Ltd. BVI (Algeria).

The investment cost in Orascom Telecommunication Tunisie and Orascom Telecommunication Algerie Spa amounted to US$ 55,065,750 and US$ 122,200,000 respectively. The fair value of these two investments in Tunisia and Algeria, based on percentage of ownership, as estimated by Standard and Poor's as of December 31, 2003 amounted to US$ 75,000,000 and US$ 185,000,000 respectively.

(24) SEGMENT INFORMATION

The following tables present revenue and profit information and certain asset and liability information regarding business segments for the year ended December 31,2003.

	Palestine Investment Fund	Palestine Commercial Services Company	American School	Tri Fitness Company	Eliminations	Total
Operating revenue	59,481,562	62,604,128	564,286	221,431	_	122,871,407
Net income (loss)	43,886,270	-2,022,494	-1,730,420	-4,718	_	40,128,638
Fixed assets	44,449,528	1,478,898	5,691,123	4,050,104	_	55,669,653
Total Assets	785,625,212	29,953,488	6,608,837	4,810,454	-27,566,697	799,431,294
Total Liabilities	71,433,944	17,516,492	2,352,424	2,250,464	-6,885,563	86,667,761

(25) RELATED PARTY TRANSACTIONS

An amount of US$ 4,573,792 due from Palestinian National Authority was outstanding as of December 31, 2003.

(26) INCOME TAX

The Palestine Investment Fund and Palestine Commercial Services Company are exempt from income tax in the Palestinian National Authority territories.

(27) CONTINGENCIES

PIF is contingently liable for costs associated with winding down the operations of some investments that were transferred by the Palestinian National Authority to the Palestine Investment Fund. The amount of liability, if any, is not quantifiable and therefore was not provided for in the attached financial statements.

Financial Performance Report

Financial
Performance

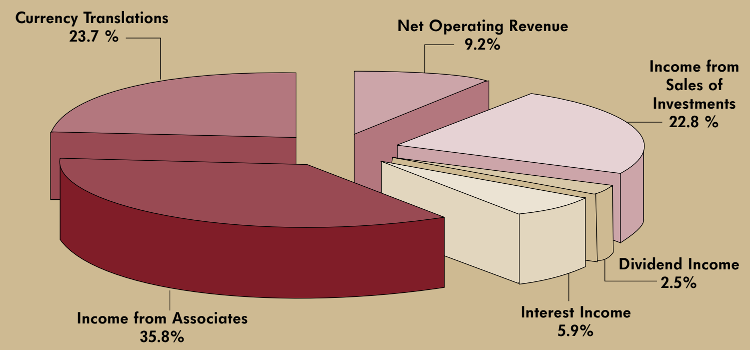
This reports briefly reviews the performance of the Palestinian Investment Fund (PIF) and in more detail, the financial statements of PIF, which include the results of its consolidated operations in Palestine as well as in other countries.

Results of Operations

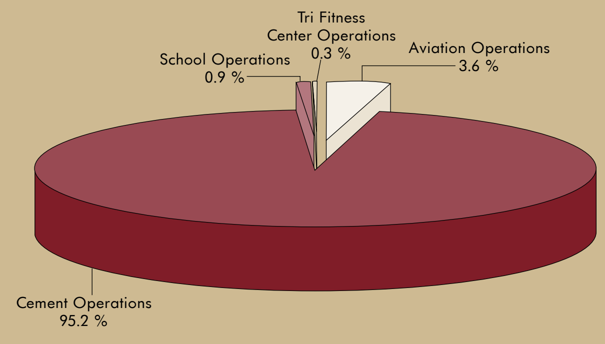
Revenue

In 2003, PIF revenues amounted to around US$ 85 million, as follows:

Revenue Breakdown



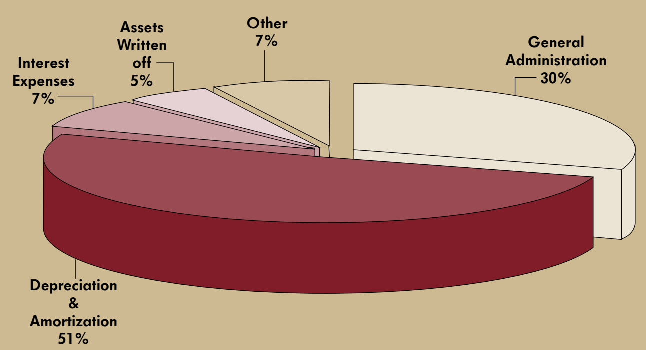
Breakdown of Operating Revenue



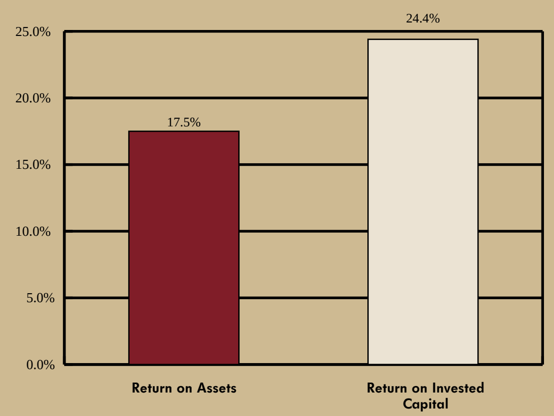
Expenses

Expenses accounted for around 43% of revenues and included the following:

Breakdown of Expenses



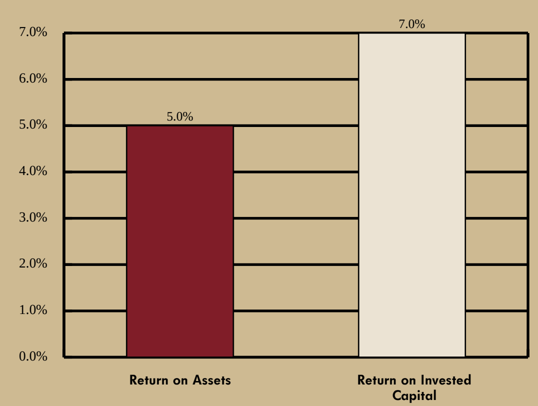
Realized + Unrealized Return on Investment



Return on Investments

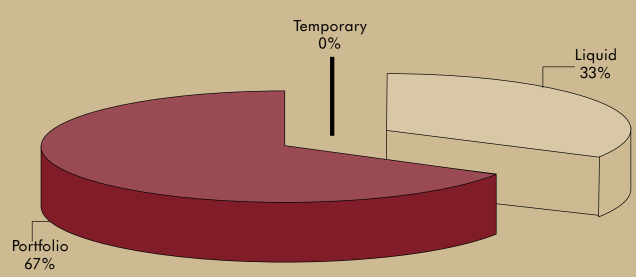
In 2003, PIF's realized and unrealized gain amounted to US$ 139,614,777, representing 24.5% return on invested capital

Realized Return on investment



In 2003 PIF net income amounted to around US$ 40 million at an earnings per share of US$ 0.07.

Investments by Type

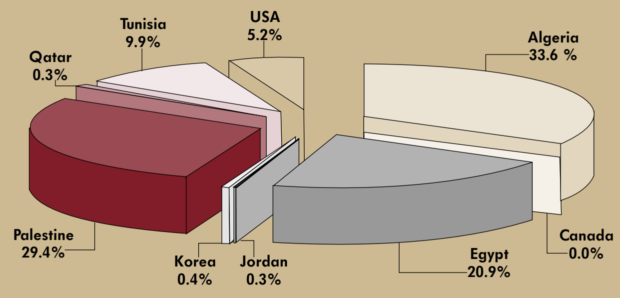


Investments

PIF's investments amounted to around US$ 570 million in 2003. The majority of these investments were in portfolios and a third was in liquid assets:

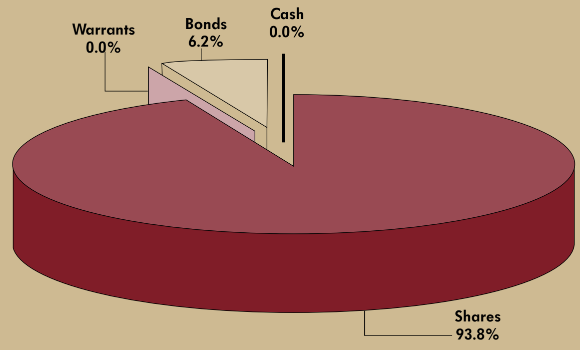
Around 34% of PIF's investments are in Algeria, followed by Palestine at around 30% and Egypt at 21%. The following chart depicts PIF's investments by country:

Investments by Country



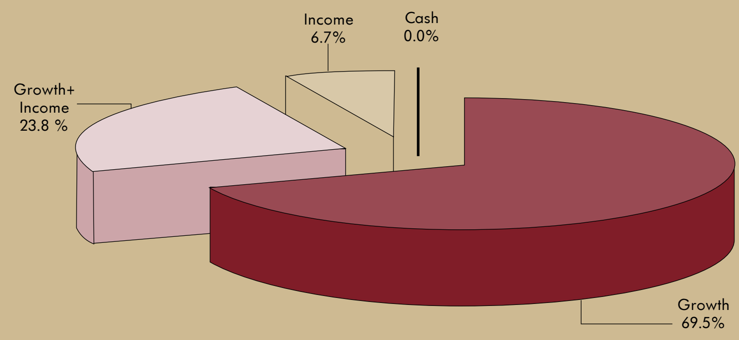
The vast majority of investments were in shares (94%) with the remainder being in bonds:

Investments by Asset Allocations

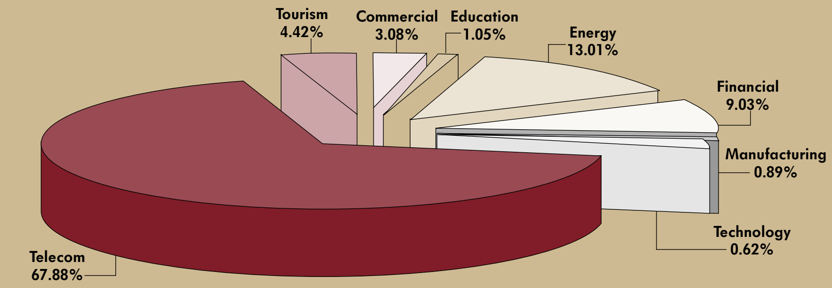


PIF's investments objectives were mainly for growth and income purposes:

Investments by Objectives

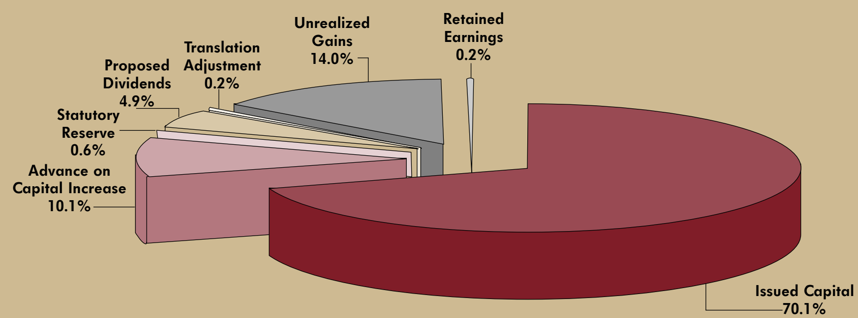


Investments by Industry



Although PIF investments are distributed among a large number of industries, the majority was in telecom, energy, and the financial sector.

Equity Components



Equity Components
In 2003, PIF equity components were as follows:

Selected Ratios

Book Value per Share	1.24
Debt to Equity	0.12
Dividend Payout Ratio	6.1%
Operating Margin	56.5%
Net Profit Margin	47.2%

Where,
* Book value per share is the ratio of net assets to weighted average number of shares
* Debt to equity is the ratio of total liabilities to total shareholders' equity
* Dividend payout is the ratio of proposed dividends to invested capital
* Operating margin is the ratio of operating profit to total revenue
* Net profit margin is the ratio of net income to total revenue

List of
Assets

	Investment Asset Name	PCSC or PA Investment	Standard & Poor's Valuation Status	Standard & Poor's Value Estimate
	Cash[1]			41,982,370
	Investments			
1	Al-Ahlia Industrial Co.	PCSC	Completed	300,000
2	Al-Tekanioon Engineering Co.	PCSC	Completed	150,000
3	"Arab Palestinian Investment Company (""APIC"")"	PCSC	Completed	6,700,000
4	Arab Palestinian Shopping Centers	PCSC	Completed	300,000
5	Aviation Project	PCSC	Completed	22,400,000
6	AVMAX Group, Inc.	PCSC	Completed	1,800,000
7	"Bioniche Life Sciences Inc. (""Bioniche"")"	PCSC	Completed	7,100,000
8	Canaan Equity II	PCSC	Completed	1,100,000
9	Canaan Equity III	PCSC	Completed	3,600,000
10	"Cap Holdings Oasis Hotel Casino Resort (""Oasis"")"	PCSC	Completed	28,510,000
11	Cement Company	PCSC	Completed	54,000,000
12	Chalcedony LLC	PCSC	Completed	4,400,000
13	Citibank Account (Venture Capital Investments)	PCSC	Completed	6,800,000
14	Convention Palace at Solomon's Pools Ltd	PCSC	Completed	2,000,000
15	Darnel Limited	PCSC	Completed	6,600,000
16	Evergreen Partners U.S. Direct Fund III, L.P.	PCSC	Completed	2,300,000
17	Gas Project (BG)	PCSC/PA	Completed	71,000,000
18	"Gaza Ahliea Insurance Company (""GAIC"")"	PCSC	Completed	1,570,000
19	Grand Park Hotel and Resorts	PCSC	Completed	100,000
20	Hanadi Tower Project	PCSC	Completed	5,000,000
21	Jerusalem Housing Project	PCSC	Completed	2,300,000
22	"Jordan Mobile Telecommunications Company, Ltd. ("JMTS" or "Fastlink")"	PCSC	Completed	66,110,000
23	Jordanian Vegetable Oil Industries	PCSC	Completed	400,000
24	Korea Investment Opportunities Ltd.	PCSC	Completed	1,500,000
25	LINKdotNET / In Touch Telecommunications Services	PCSC	Completed	8,500,000
26	National Aluminum & Profile Co.	PCSC	Completed	800,000
27	National Beverage (Coca Cola)	PCSC	Completed	1,600,000
28	"Orascom Telecom (""OT"")"	PCSC	Completed	25,240,000
29	Orascom Telecom Algeria (via its 54.711% interest in Oratel)	PCSC	Completed	90,000,000
30	Orascom Telecom Tunisia (via its 44.05% interest in Orascom Tunisia Holding and Carthage Consortium)	PCSC	Completed	50,000,000
31	"Palestine Cellular Communications Company, Ltd. ("PALCEL")"	PCSC	Completed	36,920,000
32	"Palestine Development and Investment Ltd. (""PADICO"")"	PCSC	Completed	8,700,000
33	Palestine Investment Bank	PCSC	Completed	1,600,000
34	Palestine Technology and Education Complex	PCSC	Completed	2,900,000
35	"Palestine Telecommunications Company, PLC ("PALTEL")"	PCSC	Completed	13,600,000
36	Palestine Tourism Investment Company	PCSC	Completed	2,000,000
37	Palestinian Electricity Co.	PCSC	Completed	3,000,000
38	Palestinian Flour Mills Company	PCSC	Completed	1
39	Peace Technology Fund	PCSC	Completed	2,600,000
40	Salam International Investment Company	PCSC/PA	Completed	2,400,000
41	SilverHaze Partners, LP	PCSC	Completed	260,000
42	Specialized Co. for Investment and Real Estate Development	PCSC	Completed	750,000
43	Specialized Jordanian Investments Co.	PCSC	Completed	160,000
44	The Middle East Pipes Company, Ltd.	PA	Completed	2,400,000
45	The Onyx Fund LLC	PCSC	Completed	920,000
46	The Vegetable Oil Industries Company Ltd.	PCSC	Completed	400,000
47	Tri Fitness	PCSC	Completed	3,000,000
48	United for Storage & Refrigeration	PCSC	Completed	1,800,000
49	Various Real Estate	PCSC	Completed	13,300,000
50	Yazegi Group for Soft Drinks (Pepsi)	PCSC	Completed	2,800,000
51	Al-Sharq Company (Al-Waha)	300,000	Book Value	300,000
52	Bazar Project		Book Value	100,000
53	Golden Gate Project		Book Value	150,000
54	Steel Company	PCSC	Book Value	900,000
60	Gaza Electricity & Distribution Company[3]			PA Investment(non-PCSC)

(1) US$32 Million was transferred to the Ministry of Finance for the State Budget

Standard & Poor's Report
The Democracy Council Report

STANDARD & POOR'S REPORT

February 25, 2004

Board of Directors
Palestine Investment Fund
c/o Mr. Mohamed Rachid
Managing Director
1191 Corniche El-Nil
World Trade Center, 7th Floor
Cairo, Egypt

"In spite of the present difficulties, no one should lose sight of the quality and potential of the PIF's investments in Palestine. These are all good companies with capabilities to contribute to growth in the Palestinian economy. Add to this the superlative results of the investments in other Mid-East regions in the first year of operations of the Fund, the assembly of outstanding personnel and the commitment of the Board. This is truly an incredible story to be told."

Michael C. Wierwille
Managing Director
Standard & Poors

Dear Members of the Board of Directors:

In accordance with your request, we have prepared a final report of the status of our work in connection with the valuations of the assets of the Palestine Investment Fund ("PIF" or the "Fund") as of January 1, 2003. This report covers our work since inception and summarizes our process, observations on this process, and findings to date. It has been our pleasure to be of service to you and the Fund.

Executive Summary

On September 5, 2002, the Board of Directors agreed to proceed with the valuation of all the Fund's assets as of January 1, 2003. Our work initiated with a Request for Documents that was forwarded to the management of each asset. Using the information provided, we began our analysis on October 2, 2002 examining the 69 listed assets of Palestine Commercial Services Company ("PCSC"), four direct investments of the Palestinian Authority ("PA") including Al-Bahar Company, Gaza Juice Factory, Mortgage Company and Palestine Development Company, and two jointly held assets of both PCSC and the PA, the Gas Project and Salam International Investment Company.

The valuation was conducted in two phases. Phase I ended with the issuance of a report on February 25, 2003. This phase involved the valuation of ten assets, consisting of investments in nine companies and one convertible debenture. Phase II, encompassing the remaining assets of the Fund, is complete, with certain exceptions as will be noted below.

Individual valuation reports were submitted on a rolling basis as they were finalized. As of the date of this letter, our progress through Phase II has resulted in the issuance of 49 final reports encompassing the valuations of 50 investments (the two Canaan Equity funds were consolidated for presentation purposes). The valuations of the remaining above referenced four direct investments of the PA are pending.

Finally, out of the original list of 78 assets (exclusive of cash), 20 have not been valued or were valued at their book value at the Valuation Date because either they had never begun operations, (The National Cement Manufacturing Company and The Palestinian Tunisian Company), have ceased operations or have been deemed immaterial to the Fund's balance sheet, three investments (the Electricity Monitoring and Distribution Company, General Petroleum Corporation and the Tobacco Authority) were not be valued as they will be under the control of the Ministry of Finance or need to be restructured before being qualified to become part of the PIF and one investment,
Al-Sakhra Company was not valued as it was determined by the Fund's Board of Directors that
this entity is not owned by the PA and therefore, not able to be transferred to the PIF . Attached to
this report is a summary of each asset of the Fund and its associated value as of January 1, 2003.

The valuation process has been arduous. Numerous complications were encountered including the lack of current financial statements, infrequent budgets or other pro-forma results of operations, and access to management. The interview process was also difficult and cumbersome at times, but eventually accomplished with the assistance of PIF management and staff that were invaluable in this regard.

The most difficult aspect of the valuation process, however, was treatment of the effects of the current economic and political environment (commonly referred to as the "Intifada"). The value of each investment was determined in light of its potential for recovery from the ongoing situation. Dependant on the severity of such effects, certain investments were deemed likely to recover quickly but, unfortunately, others considered that the timeframe for recovery was very long. In these latter

instances the assets were valued not as in the form of a going concern, but under an orderly liquidation setting.

In general, assets formerly held by PCSC had reasonably complete files and information eventually was available for our use. Valuations of commercial assets of the Palestinian Authority that were never owned by the PCSC and that will be transferred into the Fund will be the subject of our ongoing work next year.

The process of year-end valuation updates will begin shortly in order to provide the Board of Directors (Investment Committee) and management with a current assessment and information for the Fund's fiscal year end 2003 financial statements. This assessment will note where significant valuation changes have occurred and include certain recommendations where relevant including further investment or disposition. These recommendations, as requested, will be directed toward assisting management and the Board in their decision to further invest, divest, privatize or liquidate assets.

Political and Economic Overview

Over the last two years, the political condition in the Palestinian Territories has had a markedly negative effect on the local economy and the value of the Fundís assets. The closures and checkpoints have depressed revenues and raised costs of local companies, and subsequently increased unemployment levels throughout the region.

Gross National Income (GNI) in 2002 amounted to 40 percent less than in 2000. With a nine percent growth in the population of the West Bank and Gaza Strip ("WBGS") over the past two years, real per capita income is now only half the September 2000 level. Overall GNI losses reached US$5.4 billion after 27 months of the Intifada. Given that GNI amounted to US$5.4 billion in 1999, the opportunity cost of the crisis is now equivalent to one full year of Palestinian wealth generation.

The domestic private sector has absorbed much of the shock to the economy. Private agriculture and commercial assets have suffered over a half of all physical damage. Bank credit to the private sector is drying up, while the PA currently owes private suppliers about US$370 million. Additionally, direct donor assistance to private firms has been negligible, despite a consensus that the private sector must drive any economic recovery. Real private GDP declined by roughly 30 percent between 1999 and mid-2002.

Transportation costs have increased substantially due to the difficulties of getting around in the Palestinian Territories. Trucks and vans often are forced to use dirt tracks to circumvent checkpoints and trenches in the road. The average time needed to distribute products has tripled compared with the situation prior to September 2000. Transportation into Gaza has an additional cost element because of the multiple loading and unloading points. Further, difficultly in clearing goods at ports have led to delays in delivering products and raw materials.

The closures have had an additional impact on Gaza workers who have lost their daily jobs in Israel. Well over 50 percent of the pre-Intifada work force has been laid off. According to several new surveys conducted by the Palestinian Central Bureau of Statistics (PCBS), around 63 percent of Palestinians in the West Bank and Gaza Strip, a total of 2.5 million persons, now live below the poverty line.

The poverty levels were the highest in the Gaza Strip, standing at 84 percent, while in the West Bank levels were nearer to 54 percent. Median monthly income in the WBGS declined from 2,500 new Israeli shekels in September 2000, prior to the closures imposed by Israel, to reach NIS1,400 in March 2003. Overall, more than 47 percent of households lost 50 percent of their usual income. According to the World Bank report in March of 2002, the average per capita real income is now 30% below what it was when the Gaza-Jericho Agreement was signed in 1994.

Declining employment and income levels have inevitably depressed private consumption. The decline in households' purchasing power has made it necessary to cut back on consumption of non-essential items. People have changed their consumption habits to deal effectively with the new situation. The consumption budget for the average citizen is now focused on basic needs such as food and medicine.

The few companies in the Palestinian Territories that have continued to improve revenues and remain profitable have generally focused on exporting to neighboring Arab countries. Exports have been aided by the devaluing of the local currency (NIS), making local goods less expensive in foreign countries. Conversely, the devaluation has made it more costly for the Palestinian people and companies to purchase necessary foreign goods and equipment.

While any short-term recovery will depend on the lifting of closures, this will not suffice to put the Palestinian economy onto a sustainable growth path. The Paris Protocol, which formalized the de facto customs union with Israel that has existed since 1967, has proven extremely costly ñ and not only because of the closures that interfered with its implementation. In a structural sense (and notwithstanding the significant decline in Palestinian workers in Israel), the long-term growth potential of the Palestinian economy has been stunted by the upward pressure on domestic Palestinian wages created by wages paid to Palestinian workers in Israel. Domestic wage increases have exceeded any underlying growth in productivity, and have undermined Palestinians' ability to export competitively priced goods to the rest of the world.

Valuation Process and Findings

The most time consuming aspect of our valuation was data collection, which included conducting interviews, reviewing documentation and performing follow-up analysis. This process has been slow throughout the engagement due to delays in our receiving information from each respective investment's management. As a result, we enlisted the help of PIF staff to assist in obtaining this data to expedite future requests for information. Without their involvement, the data collection effort would have been

prolonged. In many cases, communication challenges with management and translation of documents also hindered the data collection process.

In performing our analysis, it was imperative to analyze the operating and financial results of each investment and general market data, including economic, governmental and environmental forces for each industry. In many cases, a scarcity of local industry information prompted reliance on discussions with management regarding the conditions in, and the economic outlook for, the investment's industry.

The determination of the appropriate methodology for valuing a given investment was dependent upon its potential for recovery from the effects of the Intifada. An investment's historical and projected financial results as well as its industry outlook supported the appropriate valuation treatment of each asset, whether as a going concern or under a liquidation scenario.

For purposes of this report, the majority of investments can be categorized into two groups: Companies/Projects and Investment Funds. Descriptions of the valuation methodologies used for each investment are contained in the individual valuation reports.

Companies/Projects

The category of companies and projects has been divided for presentation purposes between Palestinian and Non-Palestinian investments. The Palestinian companies are further delineated between holding companies and investments in stand-alone entities.

Palestinian Companies/Projects

The investments in Palestinian companies and projects cover the full industry spectrum including hotels and tourism, real estate, banking and insurance, telecommunications and manufacturing, among others. A significant portion of our time dealing with Palestinian companies was spent valuing the large holding companies. The holding companies, as well as their respective subsidiary companies, generally operate entirely within the Palestinian Territories.

All of our information requests and questions for the respective subsidiaries went through the management of the holding companies. The management teams of these companies were very responsive and helpful throughout the process. The professional expertise and high business acumen of the managers were made evident by the timeliness and completeness of their responses. Obtaining information and clarification on specific issues from management was more difficult for many of the stand-alone companies. In many cases, we found it necessary to contact management numerous times in order to reiterate our requests and speed up the data collection process. In this regard, the efforts of PIF management were extremely helpful. Generally, the timeliness of the receipt of information was directly proportional to the amount of control PCSC had over the company. Also, due to the less sophisticated accounting capabilities of the smaller companies, we often experienced delays in receiving vital financial information such as the 2002 financial statements.

From a technical point of view, the actual valuation of the companies operating within the Palestinian territories presented many challenges. A decline in revenues, high fixed costs and difficulties in transporting materials and goods have reduced many of the companies' profitability. The holding companies also experienced poor operating results as several of the individual companies within the group were negatively impacted by the closures and mobility restrictions in the region noted in the foregoing section. The unstable political and economic environment made predicting future operating results practically impossible. Any projections provided by management were based on assumptions about the unfolding of the current political crisis. Many of the companies have been significantly impacted, making their revenues and margins highly sensitive to the presence of peace or instability.

Several of the companies have significantly reduced their output of goods or services and postponed a number of projects indefinitely. In these cases, the companies are expected to sustain operating losses into the foreseeable future. Our findings showed that the Intifada has particularly impacted the hotel and tourism industry and the manufacturing industry.

The hotel and tourism industry in general has been subject to a devastating blow following the outbreak of confrontations since September 2000. In view of the drastic decline in the number of tourists visiting the country, occupancy rates dropped below seven percent in the first quarter of 2001 and have declined even further since then. ††††After a period during which hotels expanded their financial obligations, the sudden collapse in the industry has also caused a severe financial crisis, where most hotels in the region are defaulting on their obligations to creditors. The current crisis that confronts Palestinian hotels has prompted tourists and businessmen to seek more secure and quiet alternative locations.

The manufacturing industry in general has also faced significant challenges as a result of the conflict. The mobility restrictions in the Palestinian Territories led to delays in production and delivery resulting in an evident decrease in sales levels, as well as significantly increased clearance and storage costs. Several of the manufacturing companies were located in Nablus, which in 2002 endured 191 days of a complete blockade, further reducing profitability. A number of companies decided to halt production entirely, or until such time as the transportation barriers and added costs associated with such barriers become more manageable. The inherent uncertainties surrounding the political and economic environment in the PNA Territories magnified the unpredictability of the time these companies will resume operations.

Financial information was especially difficult to project for these troubled industries. In several cases, management provided us with two or three sets of projections, each based on specific political and economic developments. In these cases, we typically applied all sets of projections (both pessimistic and optimistic) to our analysis and weighed the results in order to arrive at our indicated value.

Due to the highly localized nature of real estate markets, we have relied

upon third-party appraisers for the values of many properties in the Fund. Appraisers in the Palestinian Territories are real estate brokers in addition to being appraisers. These appraisers build credibility with banks and lending institutions through the development of long-term relationships. Management has indicated that it has sought advice from financial institutions in order to confirm the reliability and credibility of the chosen appraisers.

Non-Palestinian Companies/Projects

All of the non-Palestinian companies/projects operate in the Middle East or North Africa except for two investments in Canada. These companies operate in a number of industries, including real estate, aerospace, food products and telecommunications, with the overwhelming majority of value of these investments being held in the latter sector (approximately 95%).

Several of these companies were large, public companies and traded on major exchanges in the Middle East and North Africa, while others were smaller public (e.g. Jordanian Vegetable Oil Industries and Salam International Investment Company) or private companies that presented valuation challenges similar to those experienced with the Palestinian companies. Where the investment was publicly traded, the efficiency of the underlying stock exchange and the trading volume of the individual company's stock influenced the weighting placed on the market capitalization versus other valuation methodologies.

In general, we faced fewer complications in the valuation process for companies outside of the Palestinian Territories. By and large, the financial structures present in these countries were far more developed and the accounting systems possessed by the respective companies were both superior and closer in line with international standards.

Overall, the non-Palestinian companies experienced operating results superior to their Palestinian counterparts. This performance was largely due to the fact that these companies operate in a much more stable political and economic environment, unhindered by the current conditions in the Palestinian markets. The net effect on the Fund of the positive performance of the non-Palestinian companies vis a vis the Palestinian investments is a shift in the balance of the aggregate value of the Fund's assets to non-Palestinian investments.

Investment Funds

The investment funds consist primarily of private equity funds, but also include a real estate joint venture and a closed-end fund. The investment funds were typically set up in either a partnership or limited liability company structure in which the Fund held its investment. All but two of these funds focused on investments in the United States market. The other two funds focused on general investments in the Korean and Palestinian markets.

We generally relied on the manager or general partner's estimates of fair market value for each of their respective investments, as these are typically provided to investors of the funds on a quarterly basis in their respective financial statements. In addition, our analysis included a review of the underlying investments, an analysis of any related operating or partnership agreements, and an economic and/or industry analysis appropriate for each investment fund. The managements of these investment funds were very responsive and helpful throughout the process. As such, the data collection process went smoothly and there were no communication or translation issues to overcome.

In general, we found that several of the funds focusing on investments in the United States have performed very poorly. These funds, including Canaan Equity II and III, Chalcedony LLC, Evergreen Fund III, SilverHaze Partners LP and Onyx Fund, primarily specialize in technology investments such as Internet infrastructure, communications, and software, among others. However, the aggregate value of these investments relative to the value of the overall Palestine Investment Fund (excluding cash) was less than 3%. These types of investments have experienced poor market fundamentals after the market correction of speculative technology companies in late 2000. The sole fund focusing on Palestinian investments also performed poorly for many of the same reasons as described in the Palestinian Companies/Projects section.

Sincerely,

By: Michael C. Wierwille
Managing Director

Attachment

The Democracy Council Report

James Prince
President, Democracy Council
11040 Santa Monica Boulevard, Suite 320
Los Angeles, California, 90025
4425 14th Street NE
Washington DC. 20017
U.S.A.

"The PIF was created as an independent agency for the benefit of the Palestinian people, to ensure that all commercial assets and investments owned by the PNA will be disclosed, managed, and monitored in a manner consistent with international standards of transparency, accountability, and good governance.

Throughout the Democracy Council's examination of financial assets and their management, including the processes of data collection and primary, real-time research, the overall tenor of the Palestinian business community was one of welcoming and recognizing that greater transparency and accountability would benefit the Palestinian economy as well as the populace in general. The management and staff of the PIF extended considerable assistance throughout the process. We view the recent expansion of the PIF professional investment management team with enthusiasm and believe that not only will they help fulfill the PIF's mandate, but also, in themselves, serve to bring additional qualified professionals back to Palestine."

James Prince
President
The Democracy Council

Introduction

The concept of consolidating the commercial assets of the Palestinian National Authority (PNA) and establishment of the Palestine Investment Fund (PIF) is a breakthrough reform effort designed to enhance transparency, accountability, and financial responsibility. It is expected that the commencement of operations by the Palestine Investment Fund and an initial examination of the assets and commercial operations of the PNA will form a base from which the PNA can promote a more transparent financial and investment management system and, thus, improve the quality of life for the Palestinian people. The PIF's stated objective, as detailed in the Articles of Association, is to promote economic growth and infrastructure development in Palestine by placing capital and expertise in strategically important and underserviced sectors. As such, the PIF management called for the consultants to help implement internationally accepted standards of transparency, administration, and investment management in the PIF.

In accordance with the request from the Board of Directors, we have prepared this summary of the status of our work with the Palestine Investment Fund.

Formation & Milestones of the Palestine Investment Fund

We were first approached about the concept of the Palestine Investment Fund in 1999. Work on the legal and operational structure of the Fund began a few months later. The initial decree signed by the President of the Palestinian National Authority establishing a consolidated company to manage the commercial assets of the PNA was signed in January 2000. The rise of the "intifada" put the project on hold until July 2002, when work resumed at a quickened pace.

In May 2000, we presented the draft Articles of Association. On 14 August 2002, the second Presidential decree codified the legal framework and approved of the final Articles of Association. Thus, effectively launching the Palestine Investment Fund.

Since the adoption of the Fund's legal framework, and operating structure and standards, we have been involved in three aspects of the Palestine Investment Fund:

* Ongoing examination of the assets consisting of a Transparency Diagnostic and financial valuation.
* Consultation and assistance to the management and board of the fund regarding development of the operations and governance.
* Consultation and assistance on the disposition and management of specific assets.

Key Achievements

The Palestine Investment Fund has achieved a considerable amount of success and objectives despite the hardships and logistical difficulties resulting from the economic downturn, violence, closures, and political upheaval.

* In addition to the Articles of Association, the Board of Directors

approved an extensive manual of Policies & Procedures. The manual served as a basis for a training seminar for the management and senior staff of the Fund. It is available on the PIF website.

* To date, we have issued, in compliance with accepted standards, valuations and transparency diagnostics on the core assets of the PNA. This will allow the PIF portfolio to be ransparently reported and included in the PNA budget.

* The Palestine Investment Fund registered a Memorandum of Incorporation with the Ministry of National Economy.

* All of the assets previously held by the PCSC, have been legally transferred to the PIF, except for eight (8) investments still in-progress. The ownership of assets previously held by the Palestinian National Authority, non-PSCS owned, are still in-process

* The Board resolved to liquidate or privatize twenty assets.

* The Ministry of Finance exerted control over the General Petroleum Corporation and has begun instituting a general restructuring and sector reform, such as: Eliminating the monopoly on engine lubricants/mineral oil; Eliminating the corruption and related activities of the GPC; Lowering the price of petroleum products to retailers; Eliminating the monopoly on the transport of products; Selling off interests in unrelated investments like Universal Computer Company; Streamlining operations; Instituting basic accounting financial controls while working towards issuing a comprehensive consolidated audit report; Significantly reducing smuggled and tampered products, etc. The resulting boost in volume translated into a significant increase in revenue going to the Ministry of Finance and an increase in the quality of petroleum products in the market.

* The Ministry of Finance assumed control over the Tobacco Authority. The restructuring removed the PNA from the commercial activities into a primary regulatory role. Note, thus the Tobacco Authority does not now qualify for entry into the PIF portfolio.

* In order to conduct operations in compliance with the new guidelines, the PIF hired a new senior investment management team largely comprised of six new staff members with relevant experience. They assumed responsibility for monitoring and analyzing investments as well as assuming a portion of the duties henceforth conducted by the General Manager.

* Ernst & Young was retained as an outside auditor. Their first report will be for year-end 2003.

* Following registration with the Ministry of National Economy, the PIF opened two new accounts with the Arab Bank. Signature authority includes approval by two members of the Board of Directors in addition to the General Manager.

* The PIF is making considerable progress in eliminating any remaining obfuscation regarding ownership of assets. For example, the offshore special purpose funds are being eliminated in favor of transparent direct investments.

* The Transparency Diagnostics and Valuation reports are uploaded to the PIF website in a timely fashion and are available for public consumption.

Transparency Diagnostic: Methodology & Procedures for Examination of the Assets

Increasing transparency is one of the greatest challenges facing developing nations. Opaque systems and decision-making inhibits good government and public accountability.

The Transparency Diagnostic provides the Palestinian National Authority and the Palestinian people with relevant information about its current investments. It also determines compliance with the basic international standards of transparent public reporting and investment-related risk management as required by the PIF Articles of Association. This Transparency Diagnostic does not address any individual investment's performance, future viability, or the strategic motivation for maintaining or altering the terms of a given investment relationship. Rather, the Transparency Diagnosticís objective is to provide the necessary information to enable the PIF to publicly disclose and thereby make transparent reported details concerning current portfolio investments.

Methodology

In order to obtain and analyze relevant information, the Democracy Council conducted primary and secondary research. The operations and presence of each business enterprise or asset were also physically verified. Bank accounts and other liquid assets were verified by primary research through contact with the financial institution or examination of the most up to date account information.

The bulk of the information was gathered directly from representatives of the listed investments and PIF officers. Interviews were also conducted with PNA officials, competitors, customers, investors, and outside stakeholders. The process of collecting data to complete the transparency diagnostic and valuation process has been more arduous and costly than expected due to violence, closures, political interference, and related measures occurring in the region.

The most labor-intensive and time consuming aspect of our valuation was data collection, which included conducting interviews and primary, real-time research - a process uncommon in the West Bank and Gaza. Generally, the overall tenor was one of welcoming and recognizing that greater transparency would benefit the Palestinian economy as well as the populace in general. Businesses generally welcomed us into their offices and workspaces, some more reluctantly than others, wary of our purpose and perspective. However, some representatives of the assets hesitated and stalled for many months, particularly those formerly held directly by the PNA through the Ministries, as well as smaller enterprises that required formal approval prior to the release of internal data. The lack of financial data, up to date statements, infrequent budgets or other pro-forma results of operations, also hindered the valuation process.

Investments in foreign countries were significantly more transparent. Documentation and public records were more accessible. Assets managed by the Palestine Commercial Services Corporation ("PCSC") generally had significantly more defined operations, complete files, accessible information,

and professional management than most private sector enterprises in Palestine. The management and staff of the PIF extended considerable assistance throughout the process.

In contrast, the majority of the assets controlled through the Ministries lacked consistent demarcation of operations, professionally prepared financial information, and clearly articulated objectives as well as a general consensus of legal mandates. As a result, the identification, gathering, and analyzing of information was exponentially more time consuming. Some of these companies are the subject of our on-going work, e.g. Al Bahar, etc.

The investments in Palestinian companies and projects cover the full spectrum of asset classes, including public securities, direct investments in operating companies, and investments in private equity and real estate funds. Compared to the operating companies, the Palestinian holding companies, e.g. APIC, PADICO, Peace Technology Fund were generally professionally managed. For their respective subsidiaries, research primarily went through the management of the holding companies.

Obtaining information and clarification on specific issues from management was more difficult for many of the stand-alone companies. In many cases, it was necessary to contact management numerous times in order to reiterate our requests and speed up the data collection process.

At completion, we will have conducted Transparency Diagnostics on approximately seventy-six (76) assets. By design, the findings of this process are more qualitative than quantitative. The primary purpose of the diagnostics was to provide the Palestinian National Authority and the Palestinian citizenry critical information regarding placement and use of their investments. However, for the objectives of this report, we categorized our findings into a summary calculation of whether the asset is "Accepted", Not Accepted" or "Accepted with Qualifications, e.g. Pending Privatization or Liquidation" for the Palestine Investment Fund.

Governance & Oversight
The Fund was created as an independent agency owned by the PNA for the benefit of the Palestinian people, to ensure that all commercial assets and investments owned by the PNA will be disclosed, managed, and monitored in a manner consistent with international standards of transparency, accountability, and good governance.

The Articles of Association for the PIF is based upon that of similar public funds in Europe and elsewhere. The stipulations detailed within the Articles include corporate governance commitments restricting conflicts of interest, instituting adequate oversight and a system of checks and balances, staffing requirements as well as such guidelines for managing the Palestinian Authority budget, making investments, undertaking due diligence reports, enforcing disclosure standards, and auditing the financial results.

The Articles further specify the role of the management and members of the Board of Directors. The PIF must be overseen by a minimum of seven and a maximum of nine Directors, a majority of whom must be from the private sector in order to ensure that the will and interests of the Palestinian people are adequately represented without undue influence. (The final Articles of Association were included in the Presidential decree of 14 August 2002. The initial Board meeting convened in October 2002. The initial directors were Samer Al-Khoury (private sector), Sabeeh Masri (private sector), Azzam Shawa (private sector), Talal Naser Al-Deen (private sector), Mohamed Rachid (management representative), Maher Al-Masri (ex-oficio public sector), and Salam Fayyad (ex oficio public sector). In compliance with the Articles of Association, the following Italics officers were elected; Chairman: Mr. Salam Fayyad, Corporate Treasurer: Mr. Azzam Al-Shawa, Corporate Secretary: Talal Naser Al-Deen. The establishment of the new government in May 2003, effectively moved Azzam Al-Shawa into the public sector, thus forcing him to vacate his seat on the Board of Directors. Subsequently, Jawdat Al-Khudari was elected as a private sector representative.

The following are the current committees and chairmen:

1- Auditing Committee:

Committee President	Dr. Salam Fayyad
Members	Jawdat Khoudary*
	Samer Khoury
	Mohamed Rachid

2- Conflicts Committee:

Committee President	Talal Nasiruddin
Members	Mohamed Rachid
	Jawdat Khoudary*

3- Investment Committee:

Committee President	Maher Masri
Members	Talal Nasiruddin
	Sabih Masri
	Mohamed Rachid
	Jawdat Khoudary*

4- Nomination Committee:

Committee President	Sabih Masri
Members	Samer Khoury
	Talal Nasiruddin
	Jawdat Khoudary*
	Mohamed Rachid

* Replaces Azzam Al-Shawa.

Assessment/Findings

With few exceptions, the existing assets examined met the "Accepted" standards of transparency and governance required by the Fund, following: 1. Acceptance of the Transparency Diagnostic by the Board of Directors, 2. Valuation by independent firm, 3. Public dissemination of the Diagnostic and Valuation reports by the Palestine Investment Fund.

The purpose of conducting the Transparency Diagnostic exercise is to identify and provide information to the Board of Directors involving the portfolio investments. Consequently, the Diagnostics identified a number of issues that, while not disqualifying the asset from inclusion into the Fund, calls for follow-on action by the board or management. We have been working with the management to streamline the investment portfolio and consolidate many of the indirect investments into transparent direct equity interests. We continue to actively work on this issue.

Ten (10) investments met the basic standards of transparency and governance necessary to entry into the PIF, however, some corrective actions need[ed] to be implemented in order to reach generally accepted standards for public investment fund For example, the Flour Mills was accepted pending resolution of the legal matters, including disposition of allegations of fraud by previous management, and a realignment of the Board of Directors. Other indirect investments were transformed and/or consolidated into publicly reported direct investments by the PIF.

Investments that do not meet the minimum standards of transparency or governance are deemed ìNot Accepted.î Such enterprises include: The General Petroleum Corporation (GPC), Gaza Electricity Monitoring & Distribution Company (GEDCo), Al Bahar, Al Sakra, and the Gaza Juice Factory.

As an example of a "Not Accepted" investment, the Transparency Diagnostic for the General Petroleum Corporation noted exceptional breaches with generally accepted standards and the assessment that a realistic description of the enterprises finances, operations, holdings, and administration could not be clearly defined. Moreover, the extent of the corruption would be considered unacceptable for a public administration. In order to facilitate the necessary internal restructuring and reform, the enterprise was annexed to the Ministry of Finance.

In March 2003, the newly appointed Minister of Energy & Natural Resources facilitated access to information enabling a basic diagnostic to be completed. The Transparency Diagnostic for GEDCo identifies the lack of controls, policies and procedures, and poor administration, as well as conflict of interests within the management, and an opaque ownership and governance structure. Our findings also concurred with other reports identifying noncompliance with current Palestinian law and/or regulations. Therefore, it is recommended that the enterprise undergo significant restructuring. When GEDCo is successfully restructured and relationship to the PNA redefined, acceptance into the PIF portfolio should be revisited.

The Gaza Juice Factory remains the single commercial asset of the PNA that refuses to comply with the dictates of the Presidential decrees establishing the Palestine Investment Fund. To be compliant with the approved standards, the Palestinian National Authority, through the PIF, should liquidate or otherwise exit out of this investment.

The consulting team has been asked to assist with the process of establishing a new, transparent and more effective logistics management program for the border sites. Karni was chosen as the model or pilot area. In response, we developed a draft Public Tender for private companies to bid on management of the site and liasoned with various donors regarding support for capital expenditures and insurance. The Cabinet resolved that the Minister of Transportation would oversee the Tender and resulting activities. The project's status is currently pending.

From a technical point of view, the actual financial research and gathering of data on companies operating within the Palestinian territories presented many challenges. The unstable political and economic environment combined with a lack of accounting, corporate, financial standards, as well as infrequent compliance with public reporting and auditing requirements forced us to conduct on-site research and work with the management to identify appropriate documentation. Given the difficult circumstances and the need to verify operations and fixed assets, we conducted a physical site examination for every investment in Palestine and the region.

Administration

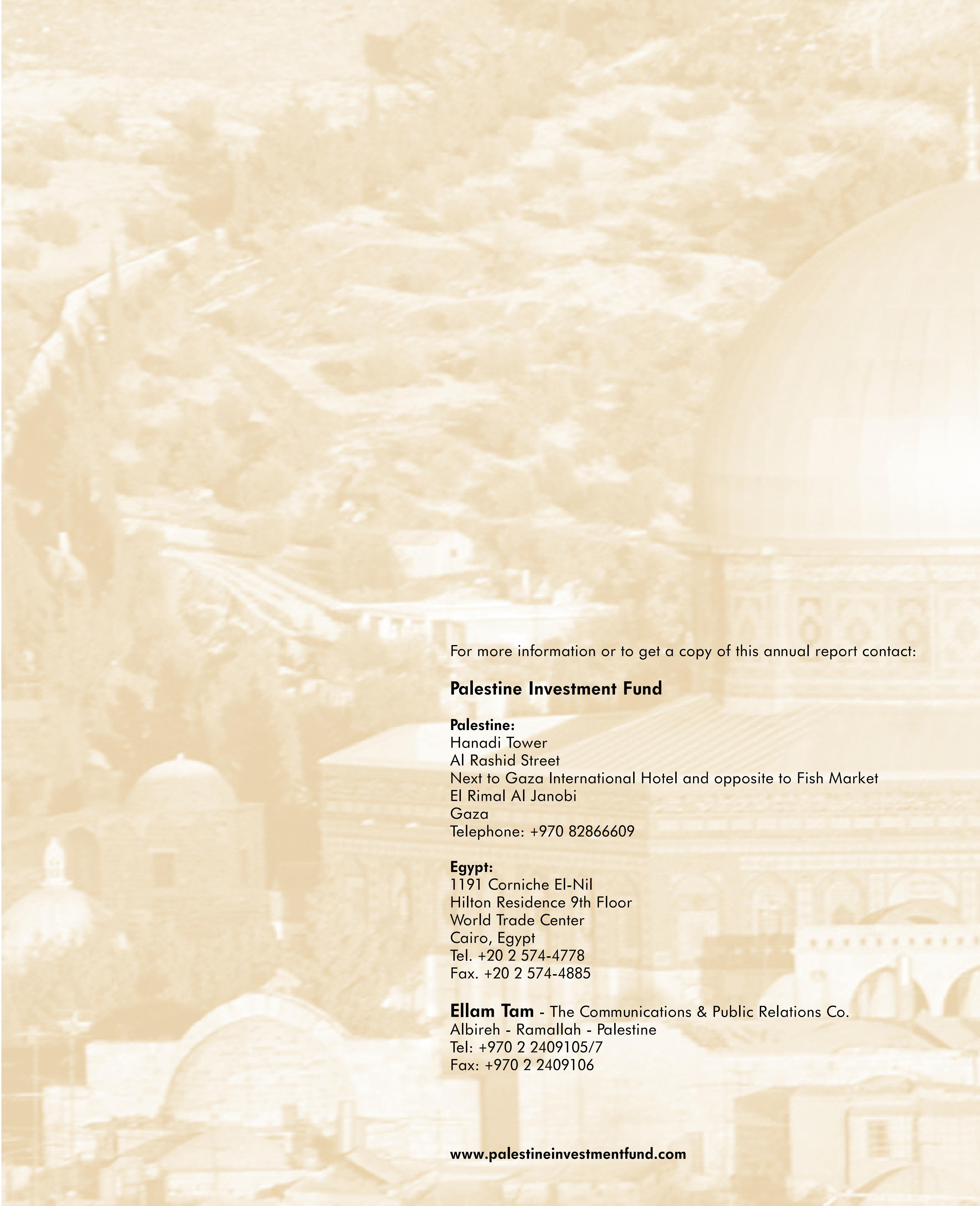
From our position as independent consultants, we continue to provide advice and assistance in the development of the operational, financial, and administrative capability of the PIF. We are working with the outside auditor and have conducted an initial training program for PIF staff in complying with the Articles of Association and Policies & Procedures Manual.

During the course of our consultations, we identified the minimum internal capabilities and skill-sets required to operate the PIF according to accepted standards of transparency, accountability, and performance. We view the recent expansion of the PIF professional investment management team with enthusiasm and believe that not only will they help fulfill the PIF's mandate, but also, in themselves, serve to bring additional qualified professionals back to Palestine.

In agreement with the PIF, the Democracy Council will continue to serve as a consultant on transparency and governance issues. For example, the Democracy Council will participate in the due diligence or new-investment consideration process to help ensure continued compliance with generally accepted standards. We also respectfully recommend that the Board of Directors begin proactive discussions on how and when to implement this process for the non-PCSC assets that do not meet the standards for acceptance into the PIF portfolio, e.g. Al Bahar, Al Sakra, gaza Juice Factory, and GEDCo..

It continues to be our privilege to work on this important project.

-End-



For more information or to get a copy of this annual report contact:

Palestine Investment Fund

Palestine:
Hanadi Tower
Al Rashid Street
Next to Gaza International Hotel and opposite to Fish Market
El Rimal Al Janobi
Gaza
Telephone: +970 82866609

Egypt:
1191 Corniche El-Nil
Hilton Residence 9th Floor
World Trade Center
Cairo, Egypt
Tel. +20 2 574-4778
Fax. +20 2 574-4885

Ellam Tam - The Communications & Public Relations Co.
Albireh - Ramallah - Palestine
Tel: +970 2 2409105/7
Fax: +970 2 2409106

www.palestineinvestmentfund.com

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